PETITION AND TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, [redacted] 1926

No. [redacted] 46

THE UNITED STATES, PETITIONER

vs.

THE CAMBRIDGE LOAN AND BUILDING COMPANY

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

PETITION FOR CERTIORARI FILED JANUARY 14, 1926
CERTIORARI GRANTED APRIL 5, 1926

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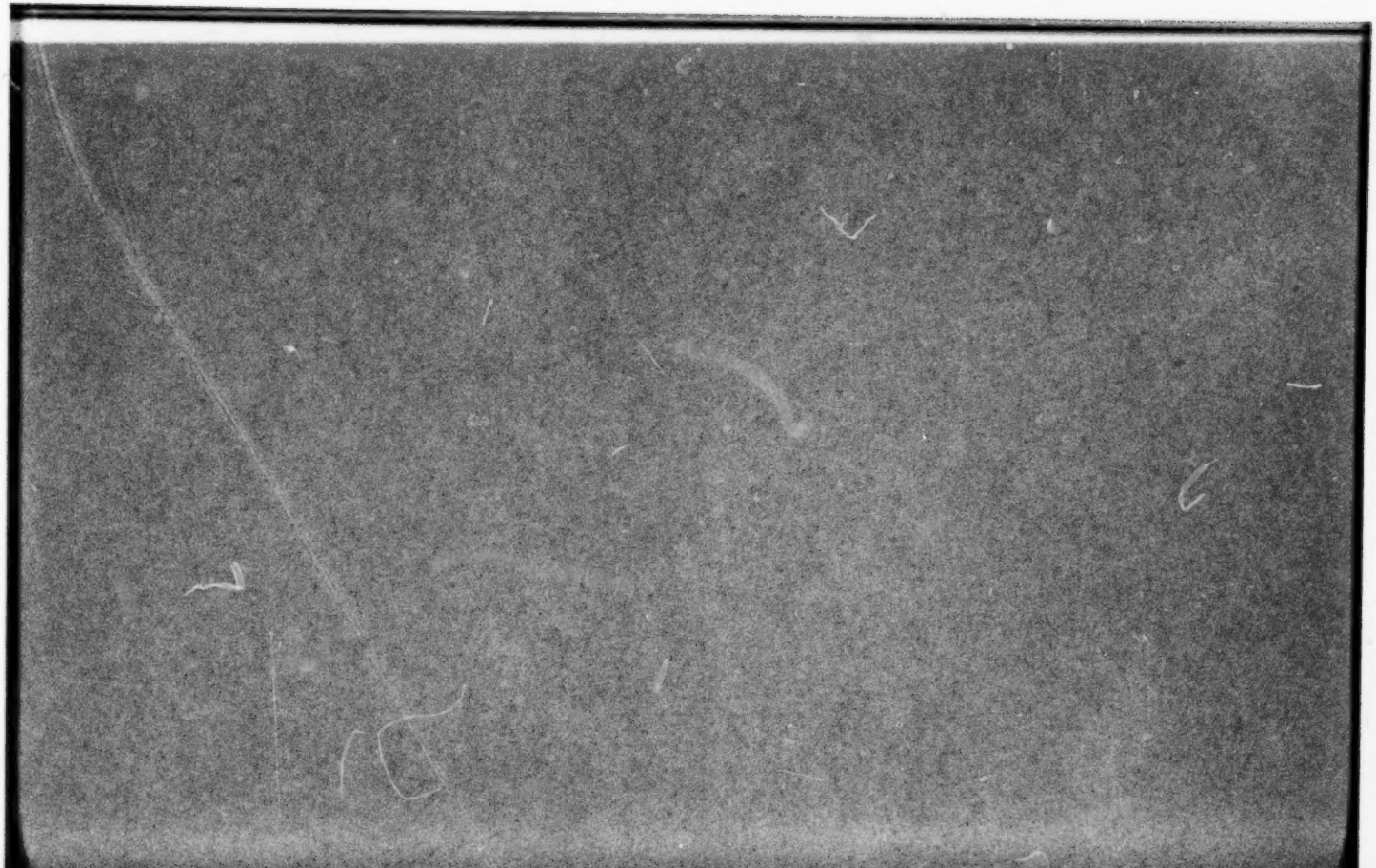

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1927

No. 700

THE UNITED STATES, PETITIONER

vs.

THE CAMBRIDGE LOAN AND BUILDING COMPANY

ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS

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1 In the Supreme Court of the United States

October term, 1927

No. ——

THE UNITED STATES OF AMERICA, PETITIONER

v.

THE CAMBRIDGE LOAN AND BUILDING COMPANY (A CORPORATION)

Petition for writ of certiorari to the Court of Claims

The Solicitor General on behalf of the United States of America prays that a writ of certiorari issue to review the judgment of the Court of Claims entered in the above-entitled cause in favor of respondent in the sum of $17,174.67 on June 6, 1927. The Government filed a motion for new trial on August 5, 1927, which was overruled by the court on October 17, 1927.

Statement

2 The question in this case is whether respondent is entitled to exemption, as a building and loan association, from income taxes under revenue acts of 1918 and 1921. Taxes for the years 1918 to 1923, inclusive, are involved. The years 1918, 1919, and 1920 are controlled by the revenue act of 1918. Under section 231 (4) of said act (40 Stat. 1076), exemption is granted to "domestic building and loan associations and cooperative banks without capital stock organized and operated for mutual purposes and without profit." The taxes for the years 1921, 1922, and 1923 are controlled by section 231 (4) of the revenue act of 1921 (42 Stat. 253), which provides that exemption should be granted to "domestic building and loan associations substantially all the business of which is confined to making loans to members."

The substance and effect of the holding of the Court of Claims is that under either act a building and loan association, recognized as such by the laws of the State under which it exists, is entitled to exemption from such Federal taxes merely because defined as a building and loan association by State law. The Government contends that under both acts a building and loan association to be entitled to exemption must conduct its business as a building and loan association in fact and not merely be designated as such under the laws of the State of its origin. The Government further contends that a building and loan association accepting large sums of money from nonmember depositors regardless of the borrowing needs of its members for the purpose of lending the same to nonmembers is in fact conducting a savings-bank business and is not entitled

3 to exemption as a building and loan association. The Government further contends that, under the 1921 act, substantially

all of the business of a building and loan association must be confined to making loans to members, and that in this case the respondent, during the years 1921, 1922, and 1923, which are controlled by the 1921 act, did a very large and substantial part of its business with nonmembers.

The findings by the Court of Claims show that the respondent was an Ohio corporation, organized under the law of that State authorizing the creation of building and loan associations; that it made its reports to and was inspected by the superintendent of the building and loan associations of the State of Ohio and invested its funds in the manner prescribed and permitted under the laws of the State of Ohio for the investment of funds of building and loan associations, reporting its investments annually to the State authorities. During the period involved the net profits of the respondent, except such as were set aside as a reserve under the State laws and retained as undivided profits, were distributed in dividends to members. The money raised by respondent during the years involved was principally from payments on stock, from deposits by nonmembers, and from interest on money temporarily deposited by it in a bank or loaned to other building and loan associations. Deposits by nonmembers were evidenced by certificates of deposit, or by pass books, and could be withdrawn upon notice, and the respondent paid interest thereon.

4 The respondent's assets and liabilities at the end of the calendar years 1918 to 1923, inclusive, are set out in the findings, and an examination thereof (Finding VII) shows in the asset columns loans on mortgage security in very substantial amounts; in all cases over 75% of the total assets of the corporation, and deposits in other building and loan associations of substantial amounts, in most cases equaling 10% of the total assets of the corporation.

In the liabilities item 6 shows deposits (from nonmembers) and accrued interest for all of the years involved. This is considerably over 50% of the total liabilities, and for the years 1921, 1922, and 1923 a successively increasing proportion.

Finding VIII shows the loans made to members and to nonmembers during each year, and an examination of this finding clearly indicates that a large part of the business of the respondent, whether considered from the standpoint of the number of borrowers or the total amount borrowed, was done with nonmembers during the years 1918, 1919, 1920, 1921, and 1922. In 1923 both the number and the amount loaned to nonmembers decreased. The Court of Claims omitted from its findings of fact a statement of mortgages purchased in substantial amounts.

The Court of Claims was requested to find these facts concerning the mortgages purchased, and such facts were based upon a stipulation of the parties before the court. The court failed to

5 make such finding. The Government again requested that such finding be made on a motion for a new trial, and the

court overruled such suggestion without comment. Further than that, as to the table concerning the year 1923, in which a great decrease in the number of nonmember borrowers is shown, a stipulation of facts before the court shows that respondent accepted large deposits from nonmembers and the evidence shows that this was done without reference to and regardless of the borrowing needs of its members. This was requested to be found as a fact, but the court failed to make such finding, and although same was requested on a motion for new trial, such motion was overruled without comment.

The Government also requested a finding as to the number of stockholders of the respondent and the number of depositors, based upon a stipulation of facts, which statement is as follows:

	1918	1919	1920	1921	1922	1923
Stockholders	1,250	1,030	1,040	1,030	1,172	901
Depositors	1,550	1,922	2,085	2,206	2,450	3,025

As to this the Court of Claims again failed to make a finding and ignored a renewed request for such finding in the motion for new trial. The Government also requested a finding of fact based upon an agreed statement of facts showing the dividends paid on run-
6 ning stock, paid-up stock, and loan stock for the various years concerned. The Court of Claims failed to make this finding and ignored a renewed request in the motion for new trial.

In explanation of the decrease in loans to nonmembers during the year 1923, the Government offered evidence which was undisputed to the effect that respondent made loans to persons who subsequently took out nominal subscriptions of one or two shares to qualify them as members, not taking the usual number of shares to equal the amount of their loans, and it was expressly testified that it was conceived this would reduce the tax liability. A finding was requested upon this, but the court made none and again ignored a renewed request in the Government's motion for new trial.

In short, the Court of Claims has failed to make a number of findings on matters fortifying the position of the United States and on which the facts were stipulated or undisputed.

While we believe that even upon the findings as made, the decision by the Court of Claims is improper and in error, it is the purpose and intention of the Government, if the writ of certiorari is granted, to make a motion for remand to the Court of Claims for findings as to these and other additional facts which the Government submits have an important bearing upon the proper determination of this case. We see no justification whatever for the failure of the Court of Claims to give the party against whom its decision went the benefit of findings on matters bearing directly on its case.

7 Assignment of errors

(1) The Court of Claims erred in rendering a judgment in favor of respondent.

(2) The Court of Claims erred in holding that the respondent was a building and loan association entitled to exemption.

(3) The Court of Claims erred in its construction and interpretation of section 231(4) of the revenue act of 1918.

(4) The Court of Claims erred in construing section 231(4) of the revenue act of 1921 to exempt the respondent although a substantial part of its business was done with nonmembers.

Reasons for granting writ

I. The decision by the Court of Claims involves a principle which affects the income taxes of a large number of so-called building and loan associations which may yet become the subject of litigation or administrative adjustment. It is not possible to segregate the companies in respect to the two acts of 1918 and 1921 by including the so-called building and loan associations which are affected under both acts. There are 1,361 so-called building and loan associations which have been taxed, and the amount of taxes collected is reported to be undoubtedly in excess of twenty-six million dollars and probably a much larger sum, a considerable part of which may have
8 to be refunded if the decision in this case is allowed to stand.

The applicable provisions of the 1921 act here involved have been reenacted in all the later revenue acts, and the question here presented is a live one under the revenue act now in force.

II. The decision of the Court of Claims is not clearly in harmony with the principles laid down in the case of Lilley Building and Loan Company v. Miller, 280 Fed. 143, affirmed, 285 Fed. 1020, certiorari denied, 262 U. S. 754, or with the decision of the Board of Tax Appeals in Johnstown Building and Loan Association, 6 B. T. A. 463.

For these reasons it is respectfully submitted that the writ of certiorari be granted.

WILLIAM D. MITCHELL,
Solicitor General.

HERMAN J. GALLOWAY,
Assistant Attorney General.

JANUARY, 1928.

10 **In the Court of Claims**

THE CAMBRIDGE LOAN AND BUILDING COMPANY (a corporation) vs. THE UNITED STATES	No. D-1083

1. Petition

Filed December 22, 1924

To the CHIEF JUSTICE AND ASSOCIATE JUSTICES OF THE COURT OF CLAIMS:

Your petitioner, the Cambridge Loan and Building Company, a corporation, respectfully represents to your honours:

I

That it is a corporation created under and existing at all times herein referred to by virtue of the laws of the State of Ohio, one of the United States of America, having its principal place of business in the said State, and at all times herein referred to it was, within the purview and meaning of the laws of the said State of Ohio, a building and loan association and conducted, carried on, and engaged in only such business as is contemplated under the laws of the said State to be carried on, conducted, or engaged in by a building and loan association.

II

The revenue act of 1918, which is the authority for the assessment of income and excess profits taxes for the calendar years 1918,
11 1919, and 1920, provides at section 231 thereof that there shall be exempt from taxation, under Title II thereof, denominated "Income tax," domestic building and loan associations; and further provides under section 304 of said act that there shall be exempt from taxation, under Title III thereof, denominated "War profits and excess profits tax," the corporations enumerated in section 231 of said act to the extent that such corporations are exempt from income tax under Title II of said act; and further provides that when used in that act the term "domestic," when applied to a corporation, means "created or organized in the United States," and that the term "United States," when used in a geographical sense, includes only the "States, the Territories of Alaska and Hawaii, and the District of Columbia."

III

Your petitioner further represents that the revenue act of 1921, which is the authority for the assessment of income taxes for the calendar years 1921, 1922, and 1923, provides at section 231 thereof that there shall be exempt from taxation under Title II of said act, which is denominated "Income tax," domestic building and loan associations substantially all the business of which is confined to making loans to members, and also provides that the term "domestic," when applied to a corporation, means "created or organized in the United States," and that the term "United States," when used in a geographical sense, includes the "States, the Territories of Alaska and Hawaii, and the District of Columbia."

IV

Your petitioner further represents that during the calendar
12 years 1921, 1922, and 1923 substantially all of its business was confined to making loans to its members.

V

Notwithstanding the facts hereinbefore set forth, all of which were at all times well known to the Commissioner of Internal Revenue, and notwithstanding the provisions of law hereinbefore referred to, the said commissioner did on, to wit, the 18th day of September, 1924, assess against your petitioner, upon assumed authority under the revenue act of 1918, the following income and excess profits taxes for the calendar years 1918, 1919, and 1920; for the calendar year 1918, $1,963.33 and $265.05 interest; for the calendar year 1919, $1,552.80 and $199.55 interest; and for the calendar year 1920, $1,879.75 and $253.76 interest; and the said commissioner did further, upon assumed authority under the revenue act of 1921, assess against your petitioner income taxes for the calendar years 1921, 1922, and 1923, as follows: For the year 1921, $2,224.91 and $309.84 interest; for the year 1922, $1,688.18; and for the year 1923, $4,377.43.

VI

Thereafter the collector of internal revenue for the 18th district of Ohio did make formal demand upon your petitioner for the payment of said taxes and did threaten the imposition of penalties and interest for failure to make payment within the time required by his demand, against all of which said assessment and collection of taxes your petitioner did duly protest, but in order to avoid the imposition of such penalties and to avoid the seizure and distraint and sale of its property by the said collector in satisfaction of such taxes
13 and penalties your petitioner did on, to wit, the 18th day of September, 1924, under specific protest, pay the said taxes to

the said collector, all of which were subsequently covered in the Treasury of the United States.

Thereafter, on, to wit, the 25th day of September, 1924, your petitioner did duly appeal to the said commissioner by filing with him its claim for refund of the whole amount of said taxes, but the said commissioner did on, to wit, the 26th day of November, 1924, reject the said claim and refused thereby to refund the said taxes to your petitioner except $922.05 of the taxes assessed for the calendar year 1922 and $1,094.36 of the taxes assessed for the calendar year 1923, leaving as the aggregate amount rejected the sum of $14,767.56.

VII

Your petitioner further avers that it has not in any way aided, abetted, or given encouragement to rebellion against the United States; that the facts set forth herein are true; that it has never assigned the said claim nor any part thereof, but has always been and is now the sole owner thereof, and that it is justly entitled to recover of and from the United States the sum of $14,767.56, together with interest thereon at the rate of six per centum per annum from the 18th day of September, 1924.

Wherefore, your petitioner prays judgment against the United States for the sum of $14,767.56 with interest as aforesaid.

THE CAMBRIDGE LOAN AND BUILDING COMPANY,
By L. L. HAMBY, *Its Attorney in Fact.*

[*Duly sworn to by L. L. Hamby; jurat omitted in printing.*]

15 *II. General traverse*

Jan. 27, 1925

No demurrer, plea, answer, counterclaim, set-off, claim of damages, demand, or defense in the premises having been entered on the part of the defendant, a general traverse is entered as provided by rule 34.

III. Argument and submission

On April 6, 1927, this case was argued and submitted on merits by Mr. L. L. Hamby for the plaintiff and by Mr. Alexander H. McCormick for the defendant.

16 *IV. Special findings of fact, conclusion of law, and opinion of the court by Moss, J.*

June 6, 1927

This case having been heard by the Court of Claims, the court, upon the evidence, makes the following

Special findings of fact

I

The plaintiff during the calendar years 1918 to 1923, inclusive, was a corporation organized in the year 1885 under and by virtue of the laws of the State of Ohio for the purpose of raising money to be loaned to its members and others and for such other purposes as were authorized by law; was authorized to issue capital stock not in excess of $1,500,000; and had its place of business in the city of Cambridge in said State. The par value of each share was $50.

II

Ever since the creation of the office of superintendent of building and loan associations under the laws of the State of Ohio in the year 1891 the plaintiff has annually filed its report to the said superintendent as a building and loan association organized, created, and doing business as such under the laws of the State of Ohio, and the plaintiff was, as such building and loan association, annually inspected by the said superintendent in the course of his official duties.

III

With the exception of an investment of $5,000 in hotel bonds, which was disapproved by the department of building and loan associations of the State of Ohio and afterwards disposed of, the plaintiff, during the calendar years 1918 to 1923, inclusive, invested its funds in the manner prescribed and permitted under the laws of the State of Ohio for the investment of funds of building and loan associations, reported its said investments annually to the superintendent of building and loan associations of the said State, and
17 received a report each year from the said department upon the conduct of its business.

IV

Section 1 of Article V of plaintiff's constitution provided as follows:

"Anyone, upon subscribing for, or in any manner becoming entitled to, or the owner of any part of the capital stock of this company shall be deemed a member thereof and a stockholder therein to the extent of the extent of the balance of his credits of record on account of said stock."

V

During the calendar year 1918 to 1923, inclusive, the net profits of the plaintiff, except that part set aside as a reserve fund under the laws of the State of Ohio and that part retained as undivided profits, were distributed semiannually in dividends at the rate of 5.7% for the year to the members of the plaintiff company only and at the said rate to all members of all classes.

VI

The money raised by the plaintiff during the calendar years 1918 to 1923, inclusive, for the purposes of its incorporation was principally from payments on stock, from deposits by nonmembers, and from interest on moneys temporarily deposited by it in bank or loaned to building and loan associations, and the extent of all such transactions was reported to the superintendent of building and loan associations of the State of Ohio in the aforesaid annual reports.

Deposits by nonmembers were evidenced by certificates of deposit or by pass books, could be withdrawn upon notice, and plaintiff paid interest thereon, on sums deposited less than six months, 3%; more than six months and less than a year, 4%; and a year, 5%.

VII

The plaintiff's assets and liabilities at the end of each calendar year, 1918 to 1923, inclusive, were as follows:

ASSETS

	1918	1919	1920	1921	1922	1923
1 Cash on hand	$55,868.16	$28,612.70	$52,660.66	$34,955.91	$43,271.95	$39,109.69
2 Loans on mortgage security	737,130.64	862,834.40	1,111,127.09	1,254,904.98	1,289,535.98	1,522,738.17
3 Loans on stock certificates or pass-book security	8,018.80	8,698.22	9,842.50	8,896.75	16,672.24	18,042.25
4 Loans on other security	17,978.00	34,020.00	27,346.42	27,614.75	35,655.25	26,760.60
5 Furniture and fixtures	200.00	265.00				500.00
6 Real estate sold on contract	750.00	750.00	750.00	750.00		
7 Real estate—office building	22,500.00	22,500.00	22,500.00	22,500.00	22,500.00	22,500.00
8 Due from borrowers for insurance and taxes	230.12	309.14	207.19	188.34	734.38	64.14
9 Bonds	16,497.50	10,762.98	25,767.80	24,279.54	5,000.00	
10 Deposits in other building and loan associations	98,800.00	147,000.00	95,000.00	55,500.00	94,000.00	181,500.00
11 Deposits in other financial institutions					10,000.00	15,000.00
Total	957,684.89	1,119,732.50	1,345,470.26	1,429,000.27	1,527,369.78	1,818,210.85

[1] Discrepancy of 40 cents not explained.

LIABILITIES

	1918	1919	1920	1921	1922	1923
1 Running stock and dividends	$219,842.85	$207,326.07	$196,473.26	$211,031.99	$158,858.99	$112,994.34
2 Loan stock and dividends	39,304.85	38,703.94	63,245.02	68,839.52	61,216.81	42,976.41
3 Credits on mortgage loans	107,785.64	104,018.30	101,511.68	161,940.61	197,584.15	231,057.22
4 Credits on real estate sold on contract	132.89	198.53	259.50	317.12		
5 Paid-up stock and dividends	45,756.00	60,711.95	92,139.00	95,235.77	111,188.55	181,240.64
6 Deposits and accrued interest	340,698.30	464,371.72	510,451.86	609,981.31	932,918.29	1,142,796.73
7 Reserve fund	14,310.00	15,760.00	18,009.75	21,702.36	23,302.36	25,182.36
8 Undivided profit fund	14,711.82	14,951.62	14,951.62	14,951.62	20,161.07	29,659.67
9 Contingent profit on real estate sold on contract	50.00	50.00	50.00	50.00		
10 Due borrowers on unfinished buildings	3,344.49	8,630.39	8,319.95	6,950.00	2,150.00	12,378.48
11 Deposits from other building and loan associations		5,000.00				
Total	957,684.89	1,119,732.50	1,345,470.26	1,429,000.27	1,527,370.18	1,818,210.85

[1] Discrepancy of 40 cents not explained.

VIII

During the years in question the plaintiff made loans to members and to nonmembers in number and amount and on security as follows:

Security	Borrowers			
	Members		Nonmembers	
	Number	Amount	Number	Amount
1919				
Bonds	53	$17,610.00	24	$30,124.00
Real estate	3	9,700.00		
Farms	6	2,825.00	10	12,000.00
Business			4	40,300.00
Chattels			1	7,500.00
Collateral	4	2,115.00	20	2,505.00
Total	66	32,250.00	59	96,629.00
1920				
Bonds	133	170,430.00	36	62,925.00
Real estate	7	12,300.00	4	4,700.00
Farms	10	9,600.00	4	11,300.00
Business			5	22,100.00
Collateral	11	1,655.00	44	30,053.70
Total	159	194,035.00	93	131,439.70
1921				
Bonds	133	164,171.43	46	104,125.00
Real estate	3	1,940.00	4	4,700.00
Farms	5	6,850.00	10	24,300.00
Business	5	12,000.00	10	94,300.00
Chattels	1	700.00		
Collateral	9	3,190.00	22	14,642.42
Total	156	190,750.43	102	232,472.42
1922				
Bonds	149	182,291.00	19	69,650.00
Real estate	9	4,700.00		
Farms	13	14,850.00	1	4,000.00
Business	9	32,500.00	9	127,100.00
Chattels			1	13,500.00
Apartments	1	5,000.00		
Collateral	9	15,750.00	27	8,391.00
Total	191	256,170.00	57	222,641.00
1923				
Bonds	117	161,105.21	4	10,000.00
Real estate	3	1,512.00		
Farms	12	12,700.00		
Business	3	3,900.00	1	94,000.00
Chattels	1	5,000.00		
Collateral	7	1,675.00	20	19,530.00
Total	143	209,992.21	25	123,530.00
1924				
Bonds	220	355,500.00	1	700.00
Real estate	13	14,900.00		
Farms	15	26,200.00		
Business	9	150,000.00		
Apartments	1	40,000.00		
Collateral	10	9,911.00	28	9,843.00
Total	273	606,111.00	29	10,543.00
1919-1925				
Mortgage	915	1,473,900.28	197	706,396.00
Collateral	43	35,799.00	146	78,014.13
Total	958	1,499,294.28	343	784,210.13

IX

At no time during the period in question did plaintiff lend money to a nonmember in preference to a member.

X

On September 18, 1924, the Commissioner of Internal Revenue assessed against the plaintiff income and excess-profits taxes for the calendar year 1918, $1,963.33 and $265.05 interest; for the calendar year 1919, $1,552.20 and $199.55 interest; for the calendar year 1920, $1,879.75 and $253.76 interest; for the calendar year 1921, $2,294.91 and $309.81 interest; for the calendar year 1922, $3,688.18; and for the calendar year 1923, $4,377.43. The collector of internal revenue for the 11th district of Ohio made formal demand upon the plaintiff for the payment of the said taxes and interest, against which the plaintiff protested. In order to avoid the imposition of penalties and the seizure, distraint, and sale of its property in satisfaction of such taxes and penalties, the plaintiff, on the 18th of September, 1924, under specific protest, paid the said taxes to the said collector and they were thereafter covered into the Treasury of the United States.

XI

On September 25, 1924, the plaintiff appealed to the Commissioner of Internal Revenue and filed with him a claim for refund of the whole amount of the aforesaid taxes and interest. On November 26, 1924, the commissioner rejected the said claim except as to $922.05 of the taxes assessed and paid for the year 1922 and $1,094.36 of the taxes assessed and paid for 1923, for which he issued certificates of overassessment, leaving as the aggregate amount rejected the sum of $14,767.56, which is still retained in the Treasury of the United States.

Conclusion of law

Upon the foregoing special findings of fact, which are made a part of the judgment herein, the court decides as a conclusion of law that plaintiff is entitled to recover the sum of $14,767.56, with interest thereon from September 18, 1924, to date of judgment, amounting to $2,407.11, an aggregate of $17,174.67.

It is therefore adjudged and ordered that the plaintiff recover of and from the United States the sum of seventeen thousand one hundred and seventy four dollars and sixty-seven cents ($17,174.67).

Opinion

Moss, Judge, delivered the opinion of the court:

This is an action by plaintiff, the Cambridge Loan and Building Company, for the recovery of the sum of $14,767.56, which it alleges

was illegally collected by the Government as income tax for the years 1918 to 1923, inclusive. Said taxes were paid under protest, and a claim for refund was duly filed with the Commissioner of Internal Revenue and was rejected on the 26th day of November, 1924.

The question for determination is whether or not plaintiff is entitled to exemption from taxes under the provisions of the revenue acts of 1918 and 1921, respectively.

Under section 231 (4) of the revenue act of 1918, 40 Stat. 1057, exemption is granted to "domestic building and loan associations and cooperative banks without capital stock organized and operated for mutual purposes and without profit."

Under section 231 (4) of the revenue act of 1921, 42 Stat. 253, exemption is granted to "domestic building and loan associations, substantially all the business of which is confined to making loans to members."

The act of 1918 is applicable to the years 1918, 1919, 1920, and from January 1 to November 23, 1921; and the act of 1921 is applicable to the period between November 23 and December 31, 1921, when the act was passed, and to the years 1922 and 1923.

Plaintiff company was organized and incorporated under the laws of the State of Ohio in 1885, and has continuously since that time been engaged in the business of a building and loan association. Its capital stock for the years 1918 to 1923, inclusive, was $1,500,000 of the par value of $50 a share.

Under the provisions of its constitution and by-laws plaintiff company was organized "for the purpose of raising money to be loaned to its members and others, and for such other purposes as are authorized by law."

It is contended by the Government that the method pursued by plaintiff in the transaction of its business was of such a character as to destroy the essential requirements of building and loan associations as contemplated by the taxing statutes involved herein.

21 In an effort to ascertain the intention of Congress in the enactment of the exemption provisions of the acts of 1918 and 1919 it is deemed important to briefly review the history of legislation on this question, as well as the current administration of the various statutes by the Internal Revenue Bureau.

The revenue act of 1909 provided that the special excise tax therein contemplated should not apply to "domestic building and loan associations organized and operated exclusively for the mutual benefit of their members." Under this act certain litigation arose, resulting in each case in decisions favorable to the taxpayer. The Internal Revenue Bureau accepted the decisions of the courts and refunded all taxes which had been collected under this act, except those taxes which had been barred by the statute of limitations. In February, 1917, Congress authorized and directed the refund of all such taxes, referring to same as taxes "illegally collected from said associations under the excise tax act of August 5, 1909."

By the act of October 3, 1913, the restrictive term "exclusively" was omitted, the act merely providing that the tax therein imposed should not apply to "domestic building and loan associations." Under this act no building and loan association was subjected to the payment of tax, nor were they required to file a tax return.

By the act of September 8, 1916, Congress provided that "there shall not be taxed under this title any income received by * * * Fourth. Domestic building and loan associations and cooperative banks without capital stock organized and operated for mutual purposes and without profit." No building and loan association was subjected to the payment of income tax under this statute, nor was any tax return required to be filed.

The 1918 act, section 231 (4) contained the same language as that employed in the 1916 act, and under this statute no income tax was assessed or collected, nor was any return required.

The act of 1921, passed November 23 of that year, modified the 1916 and 1918 acts in so far as it relates to building and loan associations in only one particular. It provided for the exemption of those associations "substantially all the business of which is confined to making loans to members."

It will be noted, therefore, that under none of the acts, except the act of 1909, was any income tax required to be paid by any building and loan association, and that the taxes paid under the 1909 act were refunded.

A proper consideration of this legislation, together with the interpretation given to it by the Internal Revenue Bureau, covering a period of many years and involving five separate legislative enactments; the elimination of the harsh provisions of the earlier act of 1909; and the refund of the taxes collected under the 1909 act would seem to indicate clearly a fixed purpose and intention on the part of Congress to exempt from taxation building and loan associations conforming in essential respects to the primary business of such associations. It was not until the early part of the year 1922, after the effective date of the act of 1921, that the Commissioner of Internal Revenue undertook to subject any building and loan association to the payment of income tax.

The Government chiefly relies in this case upon the decisions in the case of Ackline v. Peoples Savings Association, 293 Fed. 392, 22 and in the case of Lilley Building and Loan Company v. Miller, 280 Fed. 145. The opinion in the former case announced certain general principles governing the operation of building and loan associations, which are usually accepted as sound and correct, but the sole question at issue in that case was whether or not the Commissioner of Internal Revenue had authority to define the qualifications for membership, the court holding that he had no such power. The purpose of citing this case in support of the Government's contention in the case now being considered is not clear.

Under the facts in the Lilley case the court held that the association was not a true building and loan association, but was in effect

a savings bank. This action involved the years 1918, 1919, and 1920, and is therefore governed by the 1918 act. Conspicuous among the facts as they appear in the opinion are the following: Receipts of deposits from nonmembers constituted the bulk of its business. If received time deposits for which it issued certificates bearing interest at the rate of 5 per cent. The year 1920, considered as typical of the period of time involved, shows running stock of $121,000, paid-up stock of $123,000, deposits of $830,000, borrowed money $20,000, and a reserve fund of $18,500. Stockholders numbered 301 and borrowers 495, of whom only two were stockholders. It had 2,239 savings depositors. The deposits from nonmembers were evidenced by entries in books "such as are ordinarily used by savings banks." About 80 per cent of its receipts and 97 per cent of its loans were transactions with nonmembers.

A statement of the essential facts connected with the operation of plaintiff company will readily demonstrate the inapplicability of the decision in the Lilley case to the facts in the present case.

In the year 1918 forty mortgage loans were made to members and thirty-nine to nonmembers; in 1919, one hundred and fifty-eight to members and forty-seven to nonmembers; in 1920, one hundred and forty-three to members and seventy to nonmembers; in 1921, one hundred and seventy-seven to members and thirty to nonmembers; in 1922, one hundred and seventy five to members and ten to nonmembers; in 1923, two hundred and sixty two to members and one to nonmembers. Through the entire period 1918 to 1923, inclusive, nine hundred and fifty-five mortgage loans were made to members and one hundred and ninety-seven to nonmembers, the loans to members being more than 82 per cent of the total number of loans. In the Lilley case out of a total of 495 loans only two, or four-tenths of one per cent, were members or shareholders.

For the period from 1918 to 1923, inclusive, the total amount of loans was $2,271,604.40. Of this amount $1,488,294.28 was loaned to members and $783,310.12 to nonmembers. While the ratio varied from year to year, the percentage for the whole period was 66 per cent to members and 34 per cent to nonmembers.

The net profits of plaintiff company for each year, after providing for expense of operation and the reserve required under the law of the State of Ohio, were distributed semiannually, to members only, in dividends at the rate of 5.7 per cent for the year. The principal source of the earnings of the company was interest. It deposited surplus funds with other building and loan associations
from which it derived interest at the rate of 6 per cent, and
23 such deposits could be withdrawn at any time, and the earnings from these transactions likewise accrued to the benefit only of the members. It received deposits from nonmembers, evidenced by certificates of deposit or by pass books such as are in common use by building and loan associations. It paid interest on such deposits at the rate of 3 per cent, 4 per cent, and 5 per cent,

determined by the length of time for which the deposit was allowed to be retained. Such deposits constituted a portion of the fund from which loans were made at the established legal rate, and the benefit from these transactions likewise accrued to the members alone. It deposited a part of its surplus funds in other building and loan associations. We fail to see the objection to this occasional practice, as it derived an advantageous return from such deposits which accrued also to the benefit only of members; and inasmuch as these deposits could be withdrawn at any time it enabled plaintiff to carry a smaller banking balance. In making loans to nonmembers the borrowing needs of members were never neglected. So far as the record discloses, plaintiff was at all times in a position to supply the borrowing needs of its members, and at no time was a borrowing nonmember preferred over a member. A comparison of the receipts from members with the receipts or deposits from nonmembers can not be shown on account of the unsatisfactory state of the record, which seems to set forth as to this item only net balances at the end of the year. However, under our view of the whole case this information would not have a controlling influence in determining the rights of the parties.

It should be observed that in each of the acts dealing with the subject under consideration Congress has merely provided for the exemption from Federal taxation of "domestic building and loan associations" without attempting to define or describe such associations. The limitation in the 1909 act received the disapproval of Congress when it authorized and directed the taxes which had been collected under said act to be refunded, referring to same as taxes "illegally collected * * *" Inasmuch as Congress, during the period from 1909 to 1921, has deemed it proper to impose no limitation or restriction upon the exemption from taxes of building and loan associations, neither in express terms nor by defining a building and loan association, unquestionably the court is without authority to do so. In enacting these various statutes Congress was legislating with reference to building and loan associations existing and operating at the time under the various State laws. It was dealing for taxation purposes with a creature of the State, controlled and regulated by the State under its general police power. The law of the State in which they were created was the only law which described or defined a building and loan association, and Congress was chargeable with a knowledge of that law. Until the enactment of the 1921 act Congress accepted these associations as they existed and were operated in the different States; and it will be noted that in the 1921 act there was still no evident purpose of imposing any restriction upon the methods of operation further than to confine the benefits of the statute to those associations making loans substantially to members. If Congress had desired to do so it could have further restricted the exemption and limited it not only to making loans to members but also to the acceptance of deposits only from members

or to the requirement that the amount of the loan should
24 be measured by the amount of the subscription to stock and many other things complained of by the Government; but it has not thus far done so. In the absence of such legislation it is not within the authority of the court to extend or restrict the provisions of the statute. Its proper function is to construe and apply the law as it is written.

There is appended hereto as a footnote[1] a compilation of the sections of the Ohio code containing the grant of authority by the State for the operation of building and loan associations in that State. Operating under that authority and grant of powers plaintiff company has, since the year 1891, submitted an annual report to the

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[1] OHIO CODE.

Sec. 9643. *Interpretation of terms.*—A corporation for the purpose of raising money to be loaned to its members and others shall be known in this chapter and in the laws relating to the department of building and loan associations as a "building and loan association," or as a "saving association." * * *

Sec. 9644. *Receiving of deposits; trust accounts.*—To receive money on deposits, and all persons, firms, corporations and courts, their agents, officers and appointees may make such deposits and such deposits, but such corporation shall not pay interest thereon exceeding the legal rate. * * *

Sec. 9652. *Withdrawal of deposits.*—To permit withdrawal of deposits upon such terms and conditions as the association provides except by check or draft. But no such association shall be permitted to carry for any member or depositor any demand, commercial or checking account. Nothing in this chapter shall prevent members or depositors from withdrawing funds by nonnegotiable orders.

Sec. 9653. *Cancellation.*—To cancel shares and parts of shares of stock upon which the credits have been withdrawn, or upon which loans have been repaid, and release them as now stock.

Sec. 9655. *Property, leasing, holding of.*—To lease, acquire, hold, encumber, convey and rent such real estate and personal property as is necessary for the transaction of its business, or necessary to collect or protect its securities.

Sec. 9656. *Borrowing money.*—To borrow money, not exceeding twenty per cent of the assets, and issue its evidence of indebtedness or other security therefor.

Sec. 9657. *Loans; enumeration of securities.*—To make loans to members and others on such terms and conditions as may be provided by the association and upon the following securities only:

First. Obligations secured by mortgage or deed of trust on real estate or any leasehold estate therein, which mortgages or deeds of trust may be made direct to the association or they may be made to third persons or corporations and pledged by them to the association as collateral. Such obligations shall be the first liens on real estate or any leasehold estate therein, but additional loans may be made where the association holds all prior mortgage liens. Nothing herein, however, shall prevent an association organized under this act from accepting additional security other than that herein provided where the primary and principal security is a first mortgage or deed of trust on real estate or any leasehold estate therein.

Second. Obligations secured by pledge of stock in or of deposits in such association, but such loans shall not exceed either the paid up value or the withdrawal value of such stock or deposits.

Third. Obligations secured by pledge of any of the securities provided for in section 9690 of the General Code, not to exceed, however, ten per cent of the assets of the association.

Fourth. Building and loan companies that have been making loans primarily on other securities than those named in the above sections continuously since January 1, 1913, are authorized to continue the loaning on such securities.

Sec. 9660. *Investment of idle funds up to 20 per cent.*—To invest any of its idle funds, or any part thereof, in bonds or interest bearing obligations of the United States, or of the District of Columbia, or of the State of Ohio, or of any county, township, school district, or other political division in the State of Ohio, or of any incorporated city or village in the State of Ohio, or in farm loan bonds issued under the provisions of the act of Congress known as the Federal farm loan act approved July 17, 1916, and amendments thereto; and in such other securities as now are, or hereafter may be accepted by the United States to secure Government deposits in national banks. But such investments at no time shall amount in the aggregate to more than twenty per cent of the assets of such corporation.

Sec. 9662. *Consent of superintendent to sell, etc.*—To buy but not to sell, convey with the written consent previously granted by the superintendent of building and loan associations, interest bearing obligations secured by real estate mortgages which shall in all respects comply with and be within the rules adopted for making mortgage loans by the corporation making such investments. Such mortgage investments may be held and reported as mortgage loans.

Sec. 9663. *Distribution of earnings.*—To make such annual or semiannual distribution of the earnings as is hereinafter provided, and as the constitution and by-laws may prescribe.

superintendent of building and loan associations as required by law, and has received a certificate each year to the effect that it had complied with the Ohio laws relating to the conduct of its business as a building and loan association. It should be stated in this connection that during the years in question here only one objection was made by the State authorities to the methods employed by plaintiff in the operation of its business, and that had reference to a $5,000 hotel bond acquired by plaintiff as an investment. The situation was corrected in accordance with the requirement of the superintendent of building and loan associations.

It will be noted that plaintiff company was authorized to receive deposits from nonmembers and to make loans to members and nonmembers. In the decision in the Lilley case the court stated that "It is not thought that the making of loans to nonmembers, or borrowing from nonmembers, or receiving deposits to be withdrawn on demand or on time, so long as such transactions are simply incidental to the primary business of operating a mutual building and loan association, would defeat the exemption." The primary business of a building and loan association is to raise money to be loaned to its members and others.

When it is remembered that the entire benefit derived from the transactions which characterized plaintiff's business operations accrued to members alone, can it be said that those transactions resulted in the destruction or the serious impairment of the primary business of operating a building and loan association as contemplated in the taxing statutes? We think not.

During the years 1918, 1919, and 1920, and until November, 1921, plaintiff company was operating under statutes which, as stated hereinbefore, imposed no limitation whatever. No tax was collected and no tax return was required. The history of this legislation, as above outlined, together with the continuing and consistent interpretation given to those acts by the administrative officials of the Government during a period of more than twelve years, and under five successive revenue acts, if not controlling, certainly constitutes a strongly persuasive influence in a proper determination of this case. The act of 1921 exempting only such associations as confined their loans substantially to members could not affect the legal status of associations operating prior thereto and under other acts which did not even require the filing of a tax return. In attempting, after the passage of the 1921 act, to enforce the collection of taxes under prior acts the Commissioner of Internal Revenue was evidently under the impression that the exemption under the prior acts was likewise intended only for associations whose business was substantially confined to loans to members. The 1921 act is not susceptible of this construction. It was operative only upon the business of such associations after the effective date of the act. It should be stated in this connection that since the passage of the 1921 act plaintiff company has substantially complied with its provisions.

There is one other point that deserves mention. In the Lilley case the court held that the words "without capital stock organized and operated for mutual purposes and without profit" in the 1916 and 1918 acts qualified both cooperative banks and building and loan associations. The Government in this case makes the same contention, under the ruling in the Lilley case. The legislative history of the act in question easily demonstrates that such was not the intention of Congress. The House bill contained only the provision
26 for the exemption of "domestic building and loan associations." The Senate proposed an amendment providing for the exemption of "cooperative banks without capital stock organized and operated for mutual purposes and without profit * * *" The House disagreed, and the matter went to the conference committee. The explanation by the managers of the House of their agreement with the Senate is as follows: "The Senate amendment provides that the income of cooperative banks organized and operated for mutual purposes and without profit shall be exempted from the income-tax provision. The House recedes from its disagreement to the Senate amendment, with an amendment exempting cooperative banks without capital stock organized and operated for mutual purposes and without profit." It was clearly the purpose of Congress to exempt cooperative banks as described and defined in the act in addition to building and loan associations, and in the very nature of the case the qualifying language was intended to apply only to such banks. Furthermore, it is provided in article 68 of Treasury Regulations 33, promulgated under the 1916 act under the heading "unconditional," that "Among the corporations exempt from tax, without condition are * * * domestic building and loan associations * * *." In the opinion of the court the construction given to the act by the court in the Lilley case and contended for by the Government in the instant case is not sound. The qualifying language was intended to apply only to cooperative banks.

The plaintiff is entitled to judgment for the amount of taxes which have not been refunded, amounting to $14,767.56, together with interest from September 18, 1924, amounting to $2,407.11, an aggregate of $17,174.67. And it is so ordered.

HAY, Judge; BOOTH, Judge; and CAMPBELL, Chief Justice, concur.

27 *Judgment*

At a Court of Claims held in the city of Washington on the 6th day of June, A. D. 1927, judgment was ordered to be entered as follows:

The court, upon due consideration of the premises, find in favor of the plaintiff, and do adjudge and order that the plaintiff, as aforesaid, is entitled to recover and shall have and recover of and from the United States the sum of seventeen thousand one hundred seventy-four dollars and sixty-seven cents ($17,174.67).

VI. Proceedings after judgment

On August 5, 1927, the defendant filed a motion for a new trial.

On October 17, 1927, the court entered the following order on said motion:

Order

"It is ordered by the court this 17th day of October, 1927, that the defendant's motion for new trial be and the same is overruled.

28 [Clerk's certificate to foregoing omitted in printing.]

[Indorsement on cover:] File No. 33152. Court of Claims. Term No. 700. The United States, petitioner, vs. The Cambridge Loan and Building Company. Petition for writ of certiorari and exhibit thereto. Filed January 16th, 1928. File No. 33,152.

Supreme Court of the United States

Order allowing certiorari

Filed April 9, 1928

The petition herein for a writ of certiorari to the Court of Claims is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

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In the Supreme Court of the United States

OCTOBER TERM, 1927

No. 700

THE UNITED STATES, PETITIONER

v.

THE CAMBRIDGE LOAN AND BUILDING COMPANY

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI TO THE COURT OF CLAIMS

OPINION

The opinion of the Court of Claims (R. 11) is not yet reported.

JURISDICTION

The judgment of the Court of Claims was rendered on June 6, 1927 (R. 18). The United States filed a motion for new trial on August 5, 1927 (R. 19), which was overruled on October 17, 1927 (R. 19). The petition for writ of certiorari was filed on January 16, 1928 (R. 19). Jurisdiction of this court is invoked under the Act of February 13, 1925.

THE QUESTION

1. Is respondent entitled to exemption from Federal taxation under the provisions of Section 231 (4) of the Revenue Act of 1918 for the calendar years 1918, 1919, and 1920, as a domestic Building and Loan Association?

2. Is respondent entitled to exemption from Federal taxation under the provisions of Section 231 (4) of the Revenue Act of 1921 for the calendar years 1921, 1922, and 1923, as a domestic Building and Loan Association, substantially all of the business of which was confined to making loans to members?

STATUTES INVOLVED

The pertinent provision of the Revenue Act of 1918, relative to the exemption of domestic building and loan associations from income taxes and applicable to the calendar years 1918, 1919, and 1920, is to be found in Section 231 (c. 18, 40 Stat. 1057, 1076), reading as follows:

CONDITIONAL AND OTHER EXEMPTIONS

> SEC. 231. That the following organizations shall be exempt from taxation under this title [Part III—Corporations]:
>
> (4) Domestic building and loan associations and cooperative banks without capital stock organized and operated for mutual purposes and without profit.

The pertinent provision of the Revenue Act of 1921, relative to the exemption of domestic building

and loan associations from income taxes and applicable to the calendar years 1921, 1922, and 1923, is to be found in Section 231 (c. 136, 42 Stat. 227, 253), reading as follows:

> CONDITIONAL AND OTHER EXEMPTIONS OF CORPORATIONS
>
> SEC. 231. That the following organizations shall be exempt from taxation under this title [Part III—Corporations]:
>
> (4) Domestic building and loan associations substantially all the business of which is confined to making loans to members; and cooperative banks without capital stock organized and operated for mutual purposes and without profit.

STATEMENT

This is a suit to recover Federal income tax paid by respondent for the years 1918 to 1923, both inclusive. The years 1918, 1919, and 1920 are controlled by the Revenue Act of 1918, and the years 1921, 1922, and 1923 are controlled by the Revenue Act of 1921. The pertinent portions of both Acts are above set out.

The Government contends that under both Acts a building and loan association to be entitled to exemption must conduct its business as a building and loan association in fact and not merely be designated as such under the laws of the State of its origin. The Government further contends that a building and loan association accepting large

sums of money from nonmember depositors, regardless of the borrowing needs of its members, for the purpose of lending the same to nonmembers, is in fact conducting a savings-bank business and is not entitled to exemption as a building and loan association. The Government also contends that, under the Act of 1921, substantially all of the business of a building and loan association must be confined to making loans to members, and that in this case the respondent, during the years 1921, 1922, and 1923, which are controlled by the 1921 Act, did a very large and substantial part of its business with nonmembers. The Court of Claims in substance and effect held that under either Act a building and loan association recognized as such under the laws of the State of its origin is entitled to exemption under the Revenue Acts merely because defined as a building and loan association by State law. A judgment was rendered against the Government in the sum of $17,174.67, which included the taxes paid for all of said years involved and interest thereon.

The findings by the Court of Claims show that respondent was an Ohio corporation, organized under the laws of that State authorizing the creation of building and loan associations (R. 8); that it made its reports to and was inspected by the superintendent of building and loan associations of the State of Ohio and invested its funds in the manner prescribed and permitted under the laws of said State, reporting its investments annually

to the State authorities (R. 8). During the time here involved the net profits of respondent, except such as were set aside as a reserve under the State laws and retained as undivided profits, were distributed as dividends to members. (R. 8.) The money raised by respondent during the years involved was principally from payments on stock, from deposits by nonmembers, and from interest on money temporarily deposited by it in banks or loaned to other building and loan associations. (R. 9.) Deposits by nonmembers were evidenced by certificates of deposit, or by pass books, and could be withdrawn upon notice, and respondent paid interest thereon. (R. 9.)

The respondent's assets and liabilities at the end of the calendar years 1918 to 1923, inclusive, are set out in the findings. (R. 9.) Finding VII shows that during said years respondent made substantial loans to other building and loan associations. The proportion of such loans to the assets for each of said years, respectively, is as follows:

1918—10.2%; 1919—13.1%; 1920—7.2%;
1921—3.8%; 1922—6.1%; 1923—9.9%.

This statement of liabilities shows that during the same period respondent had on hand large sums of deposits and accrued interest. (R. 9.) The proportion of such deposits and interest to the total liabilities for each of said years is as follows:

1918—53.3%; 1919—59.3%; 1920—60.2%;
1921—60.8%; 1922—61%; 1923—62.8%.

Finding VIII (R. 10) shows the loans made to members and nonmembers during the period involved. If we consider the table from the standpoint of the total number of loans shown for each year, we find the proportion thereof made to nonmembers during each year as follows:

1918—57.3%;	1919—35%;	1920—40.1%;
1921—23.9%;	1922—20%;	1923— 9.6%.

If we consider it from the standpoint of the total amount of the loans shown for each year we find the proportion of loans to nonmembers as follows:

1918—75.3%;	1919—38.4%;	1920—55.4%;
1921—44.5%;	1922—35%;	1923— 1.7%.

It will be noted that the business with nonmembers materially decreased in 1923. The Government introduced evidence, which was not disputed, that respondent made loans to persons who subsequently took nominal stock subscriptions of one or two shares to qualify them as stockholders, not taking the usual number of shares to equal the amount of their loans, and it was also undisputed that it was conceived that this would reduce the tax liability. The Government requested a finding of fact to this effect, but the court failed to make such a finding.

There was a stipulation by the parties before the court showing mortgages in substantial amounts purchased by respondent. A stipulation also shows that respondent accepted large deposits from nonmembers, and the evidence shows this was done regardless of the borrowing needs of its members.

The stipulation also showed the number of depositors and the number of stockholders in the years involved, as follows:

	1918	1919	1920	1921	1922	1923
Stockholders	1,250	1,000	1,040	1,000	1,172	901
Depositors	1,550	1,922	2,085	2,200	2,410	3,025

The Court of Claims failed to make any findings upon these very material and pertinent facts though requested to do so, which request was vainly renewed in the Government's motion for new trial.

As stated in our petition for writ of certiorari, if the writ is granted we will ask this court to remand the case for full findings upon these important matters, if the facts as found are inadequate to sustain our position.

ARGUMENT

I

Respondent is not Entitled to Exemption from Federal Taxation Under the Provisions of Section 231 (4) of the Revenue Act of 1918 as a Domestic Building and Loan Association

A

The fact that a corporation is organized and operated under the building and loan laws of a state is not conclusive as to its right to exemption under section 231 (4) of the revenue act of 1918

It is well settled that a Federal tax law may not be abridged or enlarged by the force of local statutes.

United States v. *Childs*, 266 U. S. 304, 309;

N. Y., N. H. & H. R. R. Co. v. *United States*, 269 Fed. 907;

Boston and Maine R. R. v. *United States* (C. C. A. 1st), 265 Fed. 578.

The contention that a building and loan association, *eo nomine*, because organized and operating under the laws of a particular State is *ipso facto*, exempt, regardless of the fact that it has departed from the business of a true building and loan association and is in fact conducting a banking business, would, if admitted, result in a total lack of uniformity in the administration and application of the Federal statute.

Certainly Congress could not have intended that State laws and State decisions should determine the exemption or nonexemption of building and loan associations, wholly disregarding the nature and character of the business done, because permitted by State laws.

B

IT IS NOT THE NAME "BUILDING AND LOAN ASSOCIATION" WHICH IS EXEMPT UNDER SECTION 231 (6) OF THE REVENUE ACT OF 1918, BUT THE COLLECTIVE ACTIVITIES WHICH ARE ORDINARILY CARRIED ON UNDER THAT NAME

A building and loan association to be entitled to exemption from Federal taxation must be operated in accordance with the principles uniformly recognized by courts and text writers. If these recognized fundamental aims and purposes are

lacking, calling the corporation in question a "building and loan association" will not make it such in fact. It is not the name "building and loan association" which is exempt. The name is immaterial. It is the actual operations of the organization that must determine its status within the meaning of the Federal statute and it is clear that a corporation, a large part of whose business is borrowing moneys from the public for the purpose of making loans to the public for the profit of its stockholders, although permitted by the laws of a particular State so to do, thus in effect operating as an ordinary banking institution, is not entitled to exemption as a building and loan association under Federal statutes simply because so named.

The fundamental characteristics of a building and loan association.

A building and loan association is a corporation organized primarily for the purpose of enabling its members, by small periodical payments on loans made from funds contributed by its members, to build or acquire homes, and in which the members of the association share in the profits and in the losses on the basis on essential principle of mutuality, reciprocity, and equality.

> *Eversmann* v. *Schmitt*, 53 Ohio State 174;
> *Lilley Building & Loan Co.* v. *Miller*, 280 Fed. 143, Affirmed (C. C. A. 6th), 285 Fed. 1020, Certiorari denied, 262 U. S. 754;
> *Acklin* v. *Peoples Savings Association*, 293 Fed. 392;

Sundheim, Law of Building and Loan Associations (Second Edition, 1922, Sections 3 and 7);

Endlich, Law of Building Associations (Sections 1 and 7).

Respondent during the years 1918, 1919, and 1920 had departed basically and fundamentally from the primary purposes and objects of a building and loan association as generally known and recognized by the courts.

Finding VII (R. 9) of the Court of Claims shows that the bulk of respondent's funds employed in its business was not received from its members but from deposits from nonmembers, evidenced by certificates of deposit and pass books upon which it paid interest at 3, 4, 5%. (Finding VI, R. 9), which deposits and accrued interest amounted to the sum of $510,688.30 at the end of 1918, $664,371.72 at the end of 1919, and $810,451.88 at the end of 1920, the amounts increasing for the years 1921 and 1922 and reaching the sum of $1,142,796.73 at the end of the year 1923 (R. 9).

Meanwhile, as shown by the court's Finding VIII (R. 10), respondent in 1918 made 44 member loans, amounting to $32,260.00, as against 59 nonmember loans, amounting to $98,689.00; in 1919, 169 member loans, amounting to $194,035.50, as against 91 nonmember loans, amounting to $121,438.70; and in 1920, 152 member loans, amounting to $186,756.45, as against 102 nonmember loans, amounting to $232,472.42, and accepted as security homes, real estate,

farms, business property, churches, and collateral security just as would be the case in loans made by an ordinary savings and mortgage company.

Respondent in accepting large deposits from nonmembers in the years 1918, 1919, and 1920, regardless of the borrowing needs of its members and for the purpose of realizing profits from its loans to the general public, was but following the methods and practices of ordinary loan companies and banks, and was not, because thereof, entitled to exemption as a building and loan association.

When the common purpose manifest throughout Section 231 is considered, it seems clear that Congress had no intention of exempting such organizations. In no other subdivision of Section 231 has exemption been granted to organizations doing business for profit with the general public and the granting of such exemption by subdivision (4) to so-called building and loan associations would be contrary to the whole spirit and purpose of the rest of the section.

II

Substantially all of Respondent's Business During the Calendar Years 1921, 1922, and 1923 was not Confined to Making Loans to Members

Congress in enacting the exemption provisions of the Revenue Act of 1921 recognized that the primary object and purpose of a building and loan association is to raise money to be loaned to its

members, and by Section 231 (4) it provided for the exemption of only those associations "substantially *all the business* of which is confined to making loans to members," and not that substantially all of its loans shall be made to its members, which seems to be the construction placed by the Court of Claims upon this exemption provision.

The court below in its Finding of Fact VIII (R. 10) found that during the calendar years 1921, 1922, and 1923 respondent made loans to members and nonmembers in numbers and amounts as follows:

Members		Nonmembers	
Number	Amount	Number	Amount
1921—161	$256,170.00	57	$205,645.00
1922—180	209,900.35	65	113,530.00
1923—272	668,111.98	29	10,565.00

Under the above finding of the court the percentage of loan to members and nonmembers during said years was:

1921—To Members, 55.5%; To Nonmembers, 44.5%.

1922—To Members, 65%; To Nonmembers, 35%.

1923—To Members, 98.3%; To Nonmembers, 1.7%.

It was stipulated as a fact, however, by the parties that respondent purchased mortgages for investment amounting to $27,378.63 in 1921; $5,086.40 in 1922; and $14,117.50 in 1923. These amounts were excluded by the court from its Finding VIII,

and clearly constituted business done by respondent for the respective years with nonmembers.

If these amounts are included as business done with nonmembers, together with loans made to members and nonmembers as found by the court in its Finding VIII, the percentage of business done with members and nonmembers in the respective years is as follows:

1921—Members, 52.3% ; Nonmembers, 47.7%.
1922—Members, 63.9% ; Nonmembers, 36.1%.
1923—Members, 96.1% ; Nonmembers, 3.9%.

The undisputed evidence showed that after the passage of the 1921 Act requiring substantially all business to be done with members, this respondent adopted the practice of making members of those it desired to do business with by issuing to them small or nominal amounts of stock, without any relation to the extent of the association's other transactions with them. The court below failed, though asked, to make any finding covering this point.

Furthermore, the court's Finding VII (R. 9) shows that after satisfying the borrowing needs of both members and nonmembers, respondent had loaned to other building and loan associations and other financial institutions the following amounts, upon which it received interest (Finding VI, R. 9):

	1921	1922	1923
Deposits in other building and loan associations	$55,500.00	$90,000.00	$101,500.00
Deposits in other financial institutions		10,000.00	15,000.00

Petitioner requested the Court of Claims to find said amounts loaned by respondent to other building and loan associations and financial institutions as a separate finding of fact, but the court refused such separate finding and excluded said amounts from its computation of business done with nonmembers in its Finding VIII. (R. 10.)

The Government contends that such requested finding was material and that the amounts loaned by respondent for profit to other building and loan associations and other financial institutions within the meaning of said Section 231 (4) of the Revenue Act of 1921 constituted business done with nonmembers.

Including as business done with nonmembers said loans made by respondent to other building and loan associations and other financial institutions, the percentage of business done with members and nonmembers for the respective years is as follows:

1921—Members, 46.8% ; Nonmembers, 53.2%.
1922—Members, 48.5% ; Nonmembers, 51.5%.
1923—Members, 73.7% ; Nonmembers, 26.3%.

It is clear that as to the calendar years 1921 and 1922, even under the court's Finding VIII (R. 10), substantially all of respondent's business was not confined to making loans to members, and that as to the calendar year 1923 respondent was not entitled to exemption since by the purchase of mortgages and loans made for profit to other building and loan associations and other financial institu-

tions substantially all of respondent's business was not confined to making loans to members.

III

Provisions Granting Exemption from Taxation to be Construed Strictly in Favor of the Government

Respondent in this case is claiming the benefit of a special exemption from taxation granted by Congress to domestic building and loan associations, and the rule is firmly established that where an exemption from taxation is claimed the burden is upon the claimant to conclusively establish in law and in fact that it is within the terms thereof.

United States v. *Dickson*, 15 Pet. 141;
Bank of Commerce v. *Tennessee*, 161 U. S. 134, 146;
Cornell v. *Coyne*, 192 U. S. 418.

Conclusion

One of the cardinal principles which should guide a trial judge is to give the defeated party complete and fair findings of fact, so as to enable him to fairly make his points on appeal. That has not been done in this case.

There are a large number of cases similar to this pending in the courts and in the Bureau of Internal Revenue, arising under the 1918 Act and also under the 1921 Act. There are thousands of so-called building and loan associations in the United States. The provisions of the 1921 Act have been reenacted

in the later revenue Acts. A decision in this case is desirable, to guide the Treasury Department and the courts in dealing with these cases. The decision of the Court of Claims runs counter to the practice heretofore followed by the Treasury Department in dealing with these cases. The findings as they stand present a strong case for the United States, but if the Court of Claims had included in its findings additional facts established or stipulated and which the United States asked to be included the record would have been clear.

Respectfully submitted.

WILLIAM D. MITCHELL,
Solicitor General.

HERMAN J. GALLOWAY,
Assistant Attorney General.

FEBRUARY, 1928.

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In the Supreme Court of the United States

OCTOBER TERM, 1928

No. 46

THE UNITED STATES, PETITIONER

v.

THE CAMBRIDGE LOAN AND BUILDING COMPANY

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

MOTION TO REMAND

Comes now the United States, the petitioner herein, by the Solicitor General, and moves the Court to remand the above entitled cause to the Court of Claims for additional Findings of Fact as hereinafter set forth.

Your petitioner shows to the Court that this case presents the question whether respondent is entitled to exemption as a building and loan association from income taxes under the Revenue Acts of 1918 and 1921. Taxes for the years 1918 to 1923, inclusive, are involved. The years 1918, 1919, and 1920 are controlled by the Revenue Act of 1918. Under Section 231 (4) of said Act (c. 18, 40 Stat. 1057,

1076) exemption is granted to "domestic building and loan associations and cooperative banks without capital stock organized and operated for mutual purposes and without profit." The taxes for the years 1921, 1922, and 1923 are controlled by Section 231 (4) of the Revenue Act of 1921 (c. 136, 42 Stat. 227, 253) which provides that exemption should be granted to "domestic building and loan associations substantially all the business of which is confined to making loans to members."

The Court of Claims made certain Findings of Fact (R. 8-11) and concluded that the respondent was not liable for the taxes in question, and thereupon rendered a judgment against the Government in favor of said respondent for the recovery of the taxes so paid, the substance and effect of the holding of the Court of Claims being that under either Act a building and loan association, recognized as such by the laws of the State under which it exists, is entitled to exemption from such Federal taxes merely because it is defined as a building and loan association by the State laws. The Government contends that under both Acts a building and loan association, to be entitled to exemption, must conduct its business as a building and loan association in fact and not merely be designated as such under the laws of the State of its origin.

The Government contends that, upon the facts found by the Court of Claims, the judgment of said court is erroneous and should be reversed. The

Government further contends that there are additional facts, fully supported by the evidence before the Court of Claims, which are material to a proper determination of the questions presented; that it requested Findings of Fact upon said matters which the Court of Claims failed and refused to make; that it renewed its request for such findings by a motion for a new trial, which the Court of Claims overruled and again failed and refused to make such findings. The Government represents to the Court that the following facts and each of them are relevant and material and have an important bearing upon the proper determination of the question involved in this case:

1. The dividends paid on running stock, i. e., stock subscribed for to be paid for in installments, steadily decreased, while dividends on paid-up stock steadily increased.

2. Deposits were accepted in large amounts, regardless of the borrowing needs of members, for the purpose of realizing pecuniary profit by lending such deposits to nonmembers, including building and loan associations and other financial institutions, and by making investments in mortgages or other securities purchased from nonmembers.

3. The respondent was not concerned with the purpose of the borrower and did not limit its loans to those to be used for building or otherwise acquiring homes. It accepted as security for members' and nonmembers' loans mortgages on homes, real

estate, farms, business properties, churches, and apartment houses, as well as bank stock, industrial stock, municipal and other bonds.

4. Respondent's loans to members were not confined to borrowers who subscribed to stock equal to the face of the loan, but it permitted persons to become members upon subscribing to a nominal amount of stock (from one to five shares), regardless of the amount sought to be borrowed. Retroactive nominal stock subscriptions were received by respondent and, in certain cases, credits of the borrower were applied by respondent to nominal stock where no stock subscriptions had been made by the borrower.

5. The number of depositors in every year exceeded the number of stockholders, the difference being small in 1918, but thereafter being approximately twice as great in each year except 1923, when it was more than three times as great.

Wherefore, it is respectfully prayed that this Court enter an order remanding said case to the Court of Claims for findings upon each and every one of the facts above set forth and upon such further and additional facts, if any, as to this Court may seem necessary.

Respectfully submitted.

WILLIAM D. MITCHELL,
Solicitor General.

HERMAN J. GALLOWAY,
Assistant Attorney General.

BRIEF ON MOTION TO REMAND

This case involves the question whether respondent is entitled to exemption from income tax as a building and loan association under the Revenue Acts of 1918 and 1921. The years 1918 to 1923, both inclusive, are involved; the years 1918, 1919, and 1920 being governed by the Act of 1918 and the years 1921, 1922, and 1923, by the Act of 1921. The Court of Claims in substance has held that if an organization is recognized as a building and loan association under the laws of the State of its origin it is entitled to exemption from tax under the Revenue Acts. The theory of the Government is that in order to be entitled to such exemption the organization must be a building and loan association in fact and not merely in name.

The Government contends that the purposes, characteristics, and method of operation of building and loan associations in the true sense are generally known and recognized both by the lawyer and the layman. Those purposes are the raising by subscriptions of the members of a fund for making advances to members to enable them to build or buy homes. The capital funds of such associations are derived from periodical payments by members, interest and premiums paid by borrowing members,

fixed periodical installments by borrowing members, fines, forfeitures, entrance fees and fees of a similar nature, all of which go into the common treasury; and when the installment payments and profits equal the face value of the shares issued, the shares are said to mature and the face value thereof is distributed to the stockholders owning the same.

A member is entitled to borrow, on sufficient mortgage security, an amount equal to his subscription for shares, and when his shares are paid up they operate to cancel his indebtedness. Such associations are distinctly and fundamentally not money-making enterprises but are essentially mutual and cooperative. The membership consists of borrowers and lenders and the profits inure equally to such members. These associations serve a unique public purpose. They encourage thrift. They enable persons who might otherwise be unable to own their homes to become independent in that respect. And it is because of the mutual and more or less altruistic purposes that such associations have been relieved of some of the burdens imposed upon companies or organizations engaged in business for a profit.

It is the Government's theory that these things were what Congress had in mind in granting exemption from income tax liabilities to building and loan associations, and that whenever it becomes apparent that an organization has departed from the fundamental purposes, characteristics and methods

of operation of such an association, it ceases to be within the spirit, purpose, or express provisions of such exemption.

With this theory in mind, the Government urged in the Court of Claims facts which it contended show a departure by respondent in these respects. The Court of Claims made findings of fact and upon those findings of fact the Government believes the decision of that court is erroneous and must be reversed. But there were other facts which the Government feels are material and proper for consideration and determination of the questions involved. The Court of Claims failed and refused to make such findings of fact, and though the questions were again presented upon the motion for new trial, that Court again failed and refused to make findings thereon.

Each of the matters referred to in the motion to remand will now be discussed separately.

I

THE DIVIDENDS PAID ON RUNNING STOCK, I. E., STOCK SUBSCRIBED FOR TO BE PAID IN INSTALLMENTS, STEADILY DECREASED, WHILE DIVIDENDS ON PAID-UP STOCK STEADILY INCREASED

Findings of fact upon such question would have an important bearing as showing that the business was being run primarily as a money-making enterprise and for the benefit of the paid-up stockholders thereof, thus materially departing from the

fundamental purpose of mutuality underlying true building and loan associations. In Request No. VIII for Findings of Fact in the Court of Claims the Government requested the Court of Claims to find as follows:

> Claimant, during the years 1918 to 1923, inclusive, paid dividends on running stock, paid-up stock, and loan stock; as follows:

Year	Per cent	On running stock	On paid-up stock	On loan stock
1918	5	$11,555.11	$2,525.72	$1,939.58
1919	5	11,267.16	3,440.16	1,946.59
1920	6	11,174.80	3,405.17	2,259.72
1921	7	12,906.71	6,578.82	2,826.33
1922	7	10,928.55	8,579.49	2,503.40
1923	7	9,396.78	12,080.09	1,842.96

These facts were set forth as Exhibit No. 7 of an agreed statement of facts and therefore are not in dispute. In the motion for new trial (pp. 10 and 11 of such motion) the Government renewed that request and stated that obviously, with its business rapidly increasing, respondent's dividends on running stock would likewise have been steadily increasing had respondent's business been conducted in the manner of a true building and loan association, i. e., by requiring borrowers to subscribe for running or installment stock equal to the loan made. It was set out in said motion for new trial (p. 11):

> The evidence shows that plaintiff had practically ceased to issue installment stock (R. pp. 50, 51), with the evident purpose and intention of increasing the profits of its pre-

paid stockholders, and this was accomplished by accepting nominal stock subscriptions of from one to five shares.

The evidence (R. p. 55) shows plaintiff's purpose:

670. Question. You mean that at the time of the making of the loans they were not members of the association, but subsequently made application for stock loans, retroactive loans?

Answer. That is what you would call it. And in addition to that——

671. Question. And for how much were these retroactive loans? That is, the number of shares?

Answer. They were——

672. Question. One?

Answer. One and two shares.

673. Question. One and two shares, nominal subscriptions to the stock?

Answer. Nominal subscriptions.

674. Question. And what was the purpose of that, sir?

Answer. To make them members.

675. Question. To make them members?

Answer. Yes, sir.

676. Question. Because you conceived that would reduce your tax liability?

Answer. Yes, sir.

II

DEPOSITS WERE ACCEPTED IN LARGE AMOUNTS, REGARDLESS OF THE BORROWING NEEDS OF MEMBERS, FOR THE PURPOSE OF REALIZING PECUNIARY PROFITS BY LENDING SUCH DEPOSITS TO NONMEMBERS, INCLUDING BUILDING AND LOAN ASSOCIATIONS AND OTHER FINANCIAL INSTITUTIONS, AND BY MAKING INVESTMENTS IN MORTGAGES OR OTHER SECURITIES PURCHASED FROM NONMEMBERS

While substantially this same conclusion can be drawn and inferred from a consideration of the figures and tables in the findings of fact made by the Court of Claims, the matter suggested and requested is an ultimate fact which has important bearing as showing a material departure by respondent from the methods of operation of a true building and loan association.

In Request No. II for Findings of Fact the Government asked the Court of Claims to find as follows:

> During the years 1918 to 1923, inclusive, claimant did not confine its business to making loans to members, nor to loans to nonmembers in times of small demand for member loans, nor to borrowing moneys (deposits) from nonmembers for the purpose of making loans to members, but, regardless of the borrowing needs of its members, accepted large deposits from nonmembers for the purpose of realizing profits from nonmember loans, from deposits in other building and loan associations and financial institutions, and from investments in mortgages

and other securities purchased from non-members.

And in the Motion for New Trial (pp. 8 and 9 thereof) the Government again urged this matter, as follows:

> The evidence in the case at bar shows that plaintiff did not confine its business to making loans to members during any of the years 1918 to 1923, inclusive (Stipulation of Facts, Exhibit No. 3); that it borrowed large sums from nonmembers (deposits) with no reference to and regardless of the borrowing needs of its members (Stipulation of Facts, Exhibit No. 4).

The witness Deselm (secretary of Respondent) (R. p. 42) testified:

> 503. Question. Now, during your connection with the association, were deposits ever refused from nonmembers?
>
> Answer. I don't remember that they were.
>
> 504. Question. So that regardless of the borrowing needs of your members, you still continued to accept deposits from non-members?
>
> Mr. Hamby. I object to that question. His receiving deposits from nonmembers has no relation to making loans to members, but enables the association to make loans.
>
> Mr. Horton. That is all right; just answer the question.
>
> The Witness. What is the question?
>
> Mr. Hamby. Read the question to him.
>
> (Question 504 read.)

The WITNESS. Certainly; not knowing what our borrowing needs would be from day to day until the applications were made.

505. Question. But you do know what the borrowing needs of your members were?

Answer. We would not know.

506. Question. You knew what loans you were making to your members?

Answer. Yes, sir.

III

THE RESPONDENT WAS NOT CONCERNED WITH THE PURPOSE OF THE BORROWER AND DID NOT LIMIT ITS LOANS TO THOSE TO BE USED FOR BUILDING OR OTHERWISE ACQUIRING HOMES. IT ACCEPTED AS SECURITY FOR MEMBER AND NONMEMBER LOANS MORTGAGES ON HOMES, REAL ESTATE, FARMS, BUSINESS PROPERTIES, CHURCHES, AND APARTMENT HOUSES, AS WELL AS BANK STOCK, INDUSTRIAL STOCK, MUNICIPAL BONDS, AND OTHER BONDS

While the findings of fact made by the Court of Claims in the Statement of Assets and Liabilities show loans on other securities than mortgage security (Item 4 of Assets, Finding VII, R. 9), and further show (Finding VIII, R. 10) that loans were made upon all of the kinds of property enumerated in this requested finding, and therefore the truth and accuracy of the requested finding can not well be questioned, it is believed a finding of the ultimate fact of the disregard of the purpose and method of operation of a true building and loan association is material to a proper determination of this case and should be made a part of the finding

by the court below. This matter was all requested by the Government in its Request No. III for Findings of Fact before the Court of Claims.

IV

RESPONDENT'S LOANS WERE NOT CONFINED TO BORROWERS WHO SUBSCRIBED TO STOCK EQUAL TO THE FACE OF THE LOAN, BUT IT PERMITTED PERSONS TO BECOME MEMBERS UPON SUBSCRIBING TO A NOMINAL AMOUNT OF STOCK (FROM ONE TO FIVE SHARES), REGARDLESS OF THE AMOUNT SOUGHT TO BE BORROWED. RETROACTIVE NOMINAL STOCK SUBSCRIPTIONS WERE RECEIVED BY RESPONDENT, AND IN CERTAIN CASES CREDITS OF THE BORROWER WERE APPLIED BY RESPONDENT TO NOMINAL STOCK WHERE NO STOCK SUBSCRIPTIONS HAD BEEN MADE BY THE BORROWER

These facts have a most important bearing upon the Government's theory of this case. Under the 1918 Act, and especially under the 1921 Act, which contains the specific provision that substantially all of the business of the company should be confined to the making of loans to members, the percentage of business with members and the percentage with nonmembers are very important points in determining the question of respondent's right to tax exemption. And where respondent departs from the plan of a true building and loan association, which requires the shares of a borrower to equal the amount of his loan, and permits not only nominal stock subscriptions but retroactive nominal stock subscriptions, and for the purpose testified by the Secretary of the respondent:

> Question. Because you conceived that would reduce your tax liability?
>
> Answer. Yes, sir (p. 55 of the record before the Court of Claims)—

it is submitted that such facts should be in the record which this Court has before it in determining the right of respondent to such exemptions.

This matter also becomes very important as it renders misleading, to the Government's prejudice, several of the facts which were found by the Court of Claims. For instance, the court purports in Finding VIII (R. 10), to set forth a tabulation of the loans to members and nonmembers, and in such table nominal stock subscribers, as well as retroactive nominal stock subscribers, are considered as members. If these persons were considered as members and their loans considered as loans to members, only to the amount of their stock, the percentages for the latter years during which respondent engaged in this practice of nominal stock subscriptions would show a much higher percentage of business with nonmembers. The Government requested findings upon this matter in its Request No. IV and renewed that request in its motion for a new trial (p. 11 thereof), quoting in support thereof the undisputed testimony of respondent's secretary, which has heretofore been set out in connection with the discussion of Item I hereof.

V

THE NUMBER OF DEPOSITORS IN EVERY YEAR EXCEEDED THE NUMBER OF STOCKHOLDERS, THE DIFFERENCE BEING SMALL IN 1918 BUT THEREAFTER THE NUMBER OF DEPOSITORS BEING APPROXIMATELY TWICE AS GREAT AS THE NUMBER OF MEMBERS IN EACH YEAR EXCEPT 1923, WHEN IT WAS MORE THAN THREE TIMES AS GREAT

This also tends to show the true method of operation and the nature of the business being conducted by respondent, indicating clearly not only that it had departed from the business of a true building and loan association and begun that conducted by a bank, but also that its business was not substantially confined to making loans to its members. There can be no question as to the accuracy of the finding requested, since it was the subject of a stipulation of facts between the parties. The following table and statement, as pointed out in the Government's Motion for a New Trial (p. 9 thereof), shows the correctness and materiality of this request in the Motion to Remand:

> The number of stockholders and number of depositors at December 31st of the respective years were as follows (Stipulation of Facts Exhibit No. 2):

	1918	1919	1920	1921	1922	1923
Stockholders	1,270	1,600	1,940	1,900	1,172	991
Depositors	1,570	1,922	2,080	2,200	2,410	3,025

Plaintiff's nonmember business, we submit, was disproportionate to its member

business during the calendar years 1918–1919 and 1920, as shown by Stipulation of Facts Exhibit No. 3, and certainly during the calendar years 1921, 1922, and 1923, substantially all of plaintiff's business was not done with members as shown by the same Exhibit No. 3.

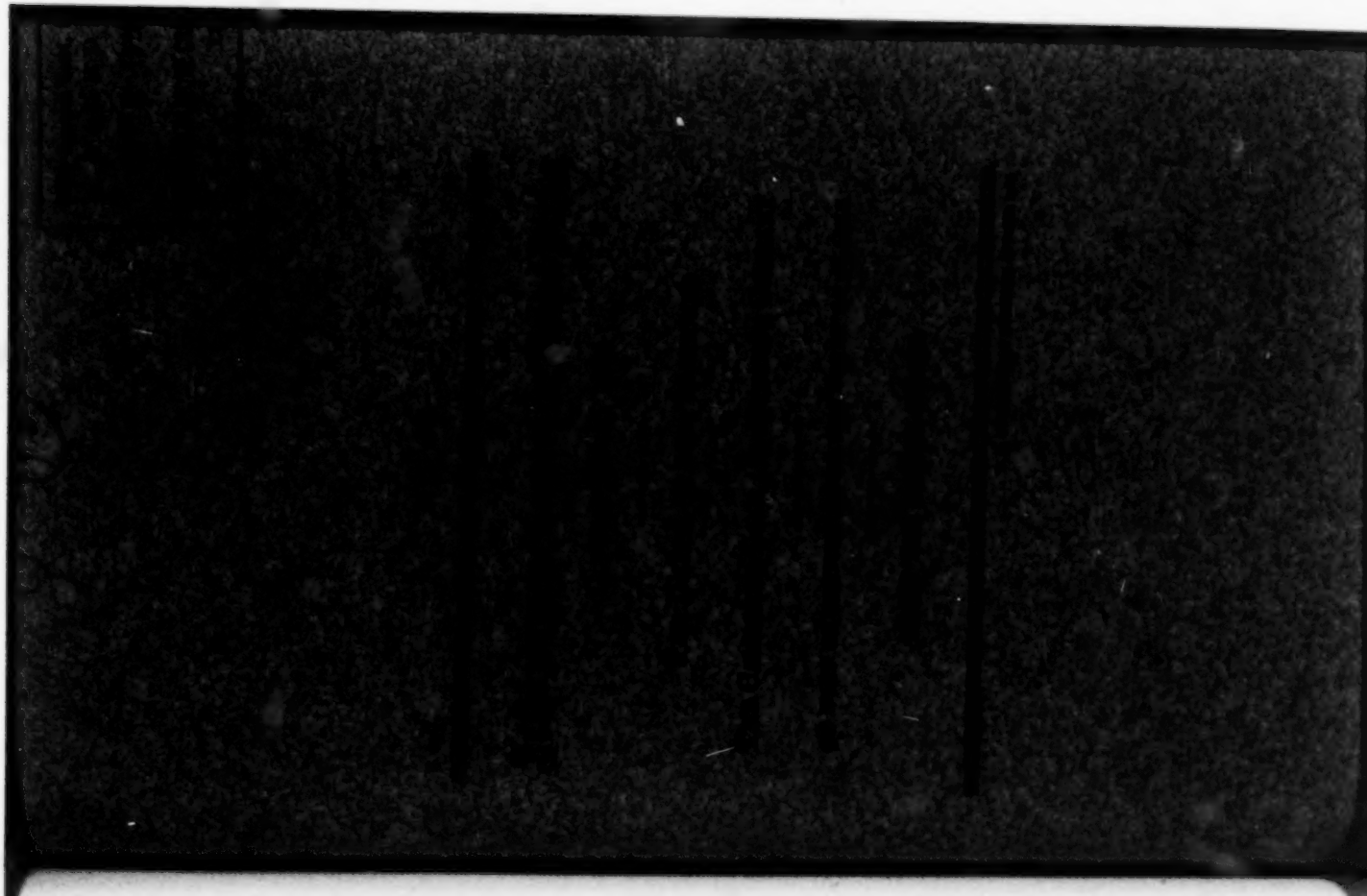
CONCLUSION

For the reasons heretofore set out it is respectfully submitted that the Government's Motion to Remand for Additional Findings of Fact should be granted.

Respectfully submitted.

WILLIAM D. MITCHELL,
Solicitor General.
HERMAN J. GALLOWAY,
Assistant Attorney General.
T. H. LEWIS,
Attorney, Bureau of Internal Revenue.

SEPTEMBER, 1928.



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In the Supreme Court of the United States

OCTOBER TERM, 1928

No. 46

THE UNITED STATES, PETITIONER

v.

THE CAMBRIDGE LOAN AND BUILDING COMPANY

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

BRIEF FOR UNITED STATES

OPINION

The opinion of the Court of Claims (R. 11–18) is reported in 63 C. Cls. 631.

JURISDICTION

The judgment was entered on June 6, 1927. (R. 18.) A motion for a new trial filed by the United States on August 5, 1927, was overruled on October 17, 1927. (R. 19.) The petition for certiorari filed by the Government on January 16, 1928 (R. 19), was granted April 9, 1928 (R. 19), under the provisions of the Act of February 13, 1925.

THE QUESTION

Is a corporation organized under the laws of the State of Ohio providing for the organization of building and loan associations and savings banks entitled to exemption from Federal taxation under the provisions of Section 231 (4) of the Revenue Acts of 1918 and 1921, respectively, where the funds which it lends are secured in a large part by accepting deposits from persons who are not members of the association and whose loans are made in a large part to persons who are not subscribers to the stock of the association?

STATUTES INVOLVED

The pertinent provision of the Revenue Act of 1918, relative to the exemption of domestic building and loan associations from income taxes and applicable to the calendar years 1918, 1919, and 1920, is to be found in Section 231 (c. 18, 40 Stat. 1057, 1076), reading as follows:

> *Conditional and other exemptions*
>
> SEC. 231. That the following organizations shall be exempt from taxation under this title (Part III—Corporations):
>
> * * * * *
>
> (4) Domestic building and loan associations and cooperative banks without capital stock organized and operated for mutual purposes and without profit.

The pertinent provision of the Revenue Act of 1921, relative to the exemption of domestic building and loan associations from income taxes and

applicable to the calendar years 1921, 1922, and 1923, is to be found in Section 231 (c. 136, 42 Stat. 227, 253), reading as follows:

> *Conditional and other exemptions of corporations*
>
> SEC. 231. That the following organizations shall be exempt from taxation under this title (Part III—Corporations):
>
> * * * * *
>
> (4) Domestic building and loan associations substantially all the business of which is confined to making loans to members; and cooperative banks without capital stock organized and operated for mutual purposes and without profit.

STATEMENT

This is a suit to recover Federal income tax paid by the respondent for the years 1918 to 1923, both inclusive. The years 1918, 1919, and 1920 are controlled by the Revenue Act of 1918, and the years 1921, 1922, and 1923, by the Revenue Act of 1921. The pertinent portions of both Acts are above set forth.

The Government contends that under both Acts a building and loan association, to be entitled to exemption, must conduct its business as a building and loan association in fact, and not merely be designated as such under the laws of the State of its origin. The Government further contends that a building and loan association accepting large sums of money from nonmember depositors, regardless

of the borrowing needs of its members, for the purpose of lending the same to nonmembers, is in fact conducting a banking business and is not entitled to exemption as a building and loan association. The Government further contends that under the Act of 1921 substantially all of the business of a building and loan association must be confined to making loans to members and that in this case the respondent, during the years 1921, 1922, and 1923, to which the Revenue Act of 1921 applies, did a very large and substantial part of its business with nonmembers. The Court of Claims in substance and in effect held that under both Acts a building and loan association organized as such under the laws of the State of its origin is entitled to exemption under the Revenue Act merely because defined as a building and loan association by State law. A judgment was rendered against the Government in the sum of $17,174.67, which included taxes paid for all of said years involved and interest thereon.

The findings by the Court of Claims show that respondent was an Ohio corporation, organized under the laws of that State authorizing the creation of building and loan associations (R. 8); that it made its reports to and was inspected by the Superintendent of Building and Loan Associations of the State of Ohio, and invested its funds in the manner prescribed and permitted under the laws of said State, reporting its investments annually to the State authorities. (R. 8.)

During the time here involved the net profits of respondent (except such as were set aside as a reserve under the State laws and retained as undivided profits) were distributed as dividends to members. (R. 8.) The money raised by respondent during the years involved was principally from payments on stock, from deposits by nonmembers, and from interest on money temporarily deposited by it in banks or loaned to other building and loan associations. (R. 9.) Deposits by nonmembers were evidenced by certificates of deposit or by pass books and could be withdrawn upon notice, and respondent paid interest thereon. (R. 9.) These deposits (Item 6 of Liabilities, Finding VII, R. 9) greatly exceeded the receipts from stock subscriptions (Items 1, 2, and 5 of Liabilities, Finding VII, R. 9) and also greatly exceeded the amounts loaned to members (Finding VIII, R. 10).

The statement of liabilities set out in the Findings of Fact shows that during the period in question respondent had on hand large deposits and accrued interest. (Item 6 of Liabilities, Finding VII, R. 9.) The proportion of such deposits and interest to the total liabilities for each of said years is as follows:

	Per cent		Per cent
1918	53.3	1921	60.8
1919	59.3	1922	61
1920	60.2	1923	62.8

Out of its funds, including these special deposits by nonmembers upon which it paid interest, respondent made loans in large sums to various

persons who were not members of the association in any sense. Finding VIII (R. 10) shows the loans made to members and nonmembers during the period involved. If we consider the table from the standpoint of the total number of loans shown for each year we find the proportion thereof made to nonmembers during each year to be as follows:

	Per cent		Per cent
1918	57.3	1921	23.9
1919	35	1922	20
1920	40.1	1923	9.6

If we consider it from the standpoint of the total amount of the loans shown for each year we find the proportion of loans to nonmembers to be as follows:

	Per cent		Per cent
1918	75.3	1921	44.5
1919	38.4	1922	35
1920	55.4	1923	1.7

The Findings also show that during said years respondent made substantial loans to other building and loan associations. (Item 10 of Assets, Finding VII, R. 9.) The proportion of such loans to the assets for each of said years, respectively, is as follows:

	Per cent		Per cent
1918	10.2	1921	3.8
1919	13.1	1922	6.1
1920	7.2	1923	9.9

If we add for these years the deposits in other building and loan associations (Item 10 of Assets, Finding VII, R. 9), the deposits in other financial institutions (Item 11 of Assets, Finding VII, R. 9), and the loans to nonmembers (Finding VIII, R. 10), we find that the percentages of such business, all

of which must have been with nonmembers, to the total loans and deposits of petitioner are as follows for the respective years:

	Per cent		Per cent
1918	85.94	1921	50.47
1919	58.04	1922	50.88
1920	63.68	1923	25.36

During the years involved the loans increased over $806,000. (Items 2, 3, and 4 of Assets, Finding VII, R. 9.) Special deposits increased over $630,000. (Item 6 of Liabilities, Finding VII, R. 9.) Paid-up stock increased over $135,000. (Item 5 of Liabilities, Finding VII, R. 9.) But loan and running stock decreased over $62,900. (Items 1 and 2 of Liabilities, Finding VII, R. 9.)

SUMMARY OF ARGUMENT

The Congress provided that building and loan associations should not be subject to the corporation income tax in order to exempt from income tax those organizations which enable persons whose earnings are small to become, by a system of compulsory savings, the owners of homesteads either at the end of a certain time or in anticipation of it. Although it did not define the term "building and loan association," Congress used this term in its ordinary significance, intending to exempt those organizations which performed a public service, but not those organizations which, though calling themselves building and loan associations, were operated for private gain.

The respondent is not such an organization as the Congress intended to exempt because its business is conducted primarily for the sake of profit and not to enable persons of small means to acquire, out of their savings, homes or other property.

The respondent clearly is not exempt under the Revenue Act of 1921 because substantially all of its business did not consist of making loans to members.

The construction and application by the Bureau of exemptions granted in prior Acts is not such a consistent and established construction as to influence the Court in construing the Acts of 1918 and 1921, and, moreover, the language of these Acts differs from the language of the prior Acts.

ARGUMENT

The term "building and loan association" refers to societies organized for the purpose of raising by subscriptions of the members a fund for making advances to members upon mortgages for the purpose of building or buying homes. The funds of such associations are derived from periodical payments by members, interest and premiums paid by borrowing members; fixed periodical installments paid by borrowing members; fines for failure to pay such fixed installments; forfeitures; fees for transferring stock; entrance fees, and any other revenues or payments, all of which go into the common treasury. When the installment payments and profits equal the face value of the shares issued the shares are said to mature and the face value

thereof is distributed to the stockholders owning same. A member is entitled to borrow on sufficient mortgage security an amount equal to his subscription for shares, and when his shares are paid up they operate to cancel his indebtedness. Although there are many plans for conducting such associations, introducing varying incidental factors, the theory of them all is that members contribute the capital and constitute the borrowers, and that the shares issued are partly paid for by members and partly earned by the operations of the association to the end that both the savings of the members and the earnings of their joint effort may be used by the members for acquiring homes. Such associations distinctly and fundamentally are not money-making enterprises. They are essentially mutual and cooperative. The membership consists of borrowers and lenders, and the profits inure equally to members, both borrowers and lenders.

Sundheim Law of Building and Loan Associations (2nd Ed., 1922) Sections 3, 7, and 17.

Endlich Law of Building Associations, Sections 1, 7.

9 Corpus Juris, 920, 921; 4 R. C. L. 343.

Eversmann v. *Schmitt*, 53 Ohio State, 174.

Such associations serve a unique public purpose. On the one hand, by means of compulsory savings they inculcate habits of thrift. On the other hand, they make it possible for those having small incomes to own homes, and thus to acquire positions in the community supposed at least to improve

their material, social, and political conditions. Their benefit to the community at large is not that the members earn more on their investment or are enabled to borrow at a low rate, because these factors are not usually present. Their benefit to the community is reflected in the elevation of the individual from a dependent to an independent status with the accompanying sense of responsibility, both as an individual and as a member of society, which accompanies home ownership. Habits of thrift and economy are established. The moral tone of the community is elevated. For that reason these organizations have been favored in law. They have been relieved from the operation of the usury laws; the liability of their members to each other and to the public has been limited and fixed by statute; they have been exempted from the operation of tax laws and other benefits have from time to time been conferred upon them.

The Government submits that it was such organizations which, for such reasons, Congress intended to exempt from the operation of the Federal income tax laws. The name "building and loan association" in common usage and in ordinary understanding connotes such associations and not associations created under statutes which enlarge the scope of operation beyond the primary purpose of such organization. In so far as that operation is enlarged, the primary public service is diminished, private interest is increased, and the basic reason for tax

exemption eliminated. Certainly Congress has indicated no intent to relieve commercial enterprises from taxation. Other corporations which are exempt from the operation of the Acts, as will appear from a reading of Section 231 of the Revenue Act of 1918, and the corresponding section (231) of the Revenue Act of 1921 are all organizations of a mutual and cooperative character which serve, or at least are thought to serve, a purpose in which the public is similarly interested.

This conclusion is strengthened by the fact that all the Acts restrict the term "building and loan association" either by the qualification that they must confine their business to making loans to their shareholders (see Section 32, Act of August 27, 1894, c. 349, 28 Stat. 509, 556; Section 17, Act of June 13, 1898, c. 448, 30 Stat. 448, 455; Section 231 (4), Revenue Act of 1921, c. 136, 42 Stat. 227, 253), or else must be organized and operated exclusively for the mutual benefit of their members. (See Section 38, Act of August 5, 1909, c. 6, 36 Stat. 11, 113, 118; Section G (a), Act of October 3, 1913, c. 16, 38 Stat. 114, 172; Section 11 (a), Revenue Act of 1916, c. 463, 39 Stat. 756, 766; Section 231 (4), Revenue Act of 1918, c. 18, 40 Stat. 1057, 1076.) The latter limitation in the Act of 1909 is unquestionable, but in the Acts of 1913, 1916, and 1918 some question has been raised by reason of the fact that organizations other than building and loan associations are named preceding the qualifying

clause. For this reason the court below holds that the qualifying phrase in the 1918 Act does not apply to building and loan associations. The contrary, however, was decided by the Circuit Court of Appeals for the 6th Circuit in *Lilley Building & Loan Company* v. *Miller*, 285 Fed. 1020 (certiorari denied, 262 U. S. 754), adopting the opinion of the District Court reported in 280 Fed. 143. It is to be observed that the Court of Claims gives an unlimited exemption to societies which call themselves building and loan associations merely because the statute omits a comma. It is submitted that this is directly in conflict with the rule laid down by this Court time and again that exemptions from taxation are to be strictly construed in favor of the Government, and ignores the principle that the words of the statute extend no further than its purpose, since such holding is not in accord with the purpose of Congress in creating exemptions.

It is true that in the Revenue Act of 1921 (Section 231 (4), c. 136, 42 Stat. 227, 253), Congress has changed the language used in the Act of 1918, but it is submitted that this change did not eliminate the necessity for that mutuality which is the fundamental characteristic of building and loan associations. In one aspect the change broadened the exemption granted by permitting the regular acquisition of funds from sources other than members if substantially all of these funds were loaned to members. In another aspect the change restricted the

exemption by eliminating those associations which did not confine their loans to members, although the reason for departing from this practice was the lack of membership applications.

The respondent in this case is not a building and loan association within this common and ordinary meaning of that term, and, therefore, is not within the spirit of the Act. Certainly the fact that it has availed itself of the right given to it by the laws of Ohio to call itself a building and loan association, and the fact that, within the laws of that State, it is treated as though it were a building and loan association do not affect the construction of the Federal Act, and do not preclude this Court from restricting the exemption to those associations which are not only in name but in fact building and loan associations. *Burk-Waggoner Oil Association* v. *Hopkins*, 269 U. S. 110. On the other hand, the incidental activities of a building and loan association, carried on to enable it to accomplish its primary purposes, would not debar it from exemption. Article 515, Regulations 45, T. D. 3179.

> *Pacific Building and Loan Association* v. *Hartson*, 201 Fed. 1011;
>
> *Parkview Building & Loan Ass'n* v. *Herold*, 203 Fed. 876;
>
> *Central Building, Loan & Savings Co.* v. *Bowland*, 216 Fed. 526.

But the respondent has not departed merely incidentally from the conduct of a building and loan association. It has departed fundamentally from

the principles and purposes of such an association and has conducted its business primarily along other lines. It is operated for the benefit of stockholders rather than members. Compare *Appeal of Johnstown Building & Loan Association*, 6 B. T. A. 463, and *Broadview Savings & Loan Co.* v. *Commissioner*, 10 B. T. A. 725.

Respondent has advanced a large part of its funds to others than members. The findings made by the court below (Finding VIII, R. 10) show that, considered from the standpoint of the total amount of loans for each year, in the year 1918 it loaned 24.64% to members and 75.36% to nonmembers. In 1919 it loaned 61.51% to members and 38.49% to nonmembers. In 1920 it advanced 44.55% to members and 55.45% to nonmembers. In 1921 it advanced 55.47% to members and 44.53% to nonmembers. In 1922 it advanced 64.90% to members and 35.10% to nonmembers. In 1923 it advanced 98.30% to members and 1.70% to nonmembers. It should be pointed out, however, that, as to the later years, and especially as to the year 1923, this figure is misleading, for the reason that during said year respondent considered as members persons who took loans and then subscribed to a nominal number of shares of stock, such as one or five shares; their stock subscriptions having no relation whatsoever to the amount of their loans.

As heretofore shown in the Statement of Facts, if we consider Finding VIII (R. 10) from the standpoint of the number of loans we find the percent-

ages of such loans to nonmembers during each year to be:

	Per cent		Per cent
1918	57.3	1921	23.9
1919	35	1922	20
1920	40.1	1923	9.6

And again, as to this statement it should be pointed out that the figures for the later years, and especially 1923, are misleading because of the nominal stock subscriptions permitted during said years, such stock subscriptions having no relation to the amount of the loans. It was also heretofore pointed out in the Statement of Facts that, if we consider this question from the standpoint of the aggregate of the deposits in other building and loan associations and financial institutions and the loans to nonmembers, we find that the percentage of such business with nonmembers for the respective years involved is as follows:

	Per cent		Per cent
1918	85.94	1921	50.47
1919	58.04	1922	50.88
1920	63.68	1923	25.36

These figures for the later years, and especially 1923, are also misleading in that persons having nominal stock subscriptions are considered as members in such figures.

The funds thus loaned were derived, in a substantial part at least (Item 6 of Liabilities, Finding VII, R 9), by accepting time deposits from persons who were not members of the association.

Heretofore in the Statement of Facts it has been shown that such deposits for the respective years

constituted the following percentages of the total liabilities of said company:

	Per cent		Per cent
1918	53.3	1921	60.8
1919	59.3	1922	61
1920	60.2	1923	62.8

and that during such period the deposits greatly exceeded the receipts from stock subscriptions and also greatly exceeded the amount loaned to members. The Statement of Facts with appropriate references to the record also shows that during the years involved the loans increased by about $806,000; the special deposits increased over $630,000; the paid up stock increased over $135,000; while the loan and running stock decreased over $62,900. These facts show conclusively that the deposits were far in excess of the requirements of borrowing members and were accepted, not for the purpose of accomodating such members, but solely for the purpose of making money. The record shows that a large part of the profits which the members received were made by dealings with others than members and that the business must have been conducted primarily for pecuniary gain and not for mutual benefit. Should we add to this the fact requested in the Government's motion to remand, which the Court of Claims failed to find and which was the subject of an agreed statement of facts before the Court of Claims, that the dividends on running stock steadily decreased from 1918 to 1923, with the exception of one year (1921), while the dividends on paid up stock steadily in-

creased (the dividends in 1918 on paid up stock amounted to $2,521.72 and in 1923 to $12,089.09), the Government's contention that this company had ceased to be a building and loan association in the true sense of the word is further fortified. Such paid up stock has been said to be contrary to the genius and purpose of a building and loan association.

> *Rhodes* v. *Missouri Savings & Loan Company*, 173 Ill. 621.
>
> *Eversmann* v. *Schmitt*, *supra*.
>
> *Leahy* v. *National Building & Loan Ass'n.*, 100 Wis. 555.

The Court of Claims states in its opinion (R. 14–15) that the deposit of surplus funds with other building and loan associations and the acceptance of deposits and the making of loans to nonmembers resulted in "benefits" which accrued to members only and that there was no objection "to this occasional practice," since the borrowing needs of the members were always taken care of. This statement not only overlooks the fact that the practice was not occasional, but was the customary course of conducting the business, but also overlooks the inherent nature of a building and loan association. Such an association is not organized to make money for its members. The excuse for its being is that a certain end may be obtained, and that end is by cooperation to accumulate a fund to be loaned to members, for the purpose of building or acquiring homes.

The Court of Claims found that the net profits were distributed by way of dividends to members

only. (R. 8.) The court considered all of the stockholders to constitute the membership of the association. Generally this is true, but in the case at bar it leads to confusion because it is indicated by the opinion of the Court of Claims (R. 16), and, as heretofore pointed out, it is conclusively shown by the findings requested but refused, and which findings are made in part the subject of a motion in this Court to remand, that the borrowing members were not limited to loans equalling their subscriptions. This situation also renders Finding VIII (R. 10) misleading in its classifications of loans to members and nonmembers, especially as to the latter years involved.

A loan in excess of the stock subscription is not, as to that excess, a loan to a member in the ordinary sense, because the profits of the association do not operate to reduce it. "One of the main justifications for building associations is the fact that the earnings are social assets, to be divided among the membership so that while a borrowing member is required to pay interest, premium and fines, a large portion being an equal share thereof is returned to him in the shape of dividends." *Gray* v. *Baltimore Building & Loan Ass'n.*, 48 W. Va. 164; *People* v. *Preston*, 140 N. Y. 549.

In administering the various tax laws providing an exemption for building and loan associations the practice of the Bureau of Internal Revenue has been neither consistent nor long continued. The regulations were changed from time to time (See

Appendix hereto, p. 21) to meet the rules laid down by the courts. But under none of them was the exemption allowed, as the Court of Claims in its opinion (R. 13) seems to suppose, to every organization calling itself a building and loan association. Under the regulations promulgated under the 1918 Act (Regulations 45, 1920 Ed., Art. 515, T. D. 3179, Appendix, p. 25) collections were made from associations conducting their business in the manner which the respondent conducts its business. These regulations were enforced prior to the passage of the Revenue Act of 1921, as is disclosed by the date of their promulgation.

The change of the language in the 1921 Act, as has been pointed out, broadened the exemption in that, under the 1921 Act, the operations of a building and loan association in regard to the securing of money were immaterial provided substantially all its loans were made to members. The respondent in this case might, therefore, come within the 1921 Act if it appeared that its loans were substantially all made to its members. The record heretofore discussed discloses this was not the fact. As has been previously pointed out, Finding VIII of the Court of Claims as to the amount of loans made to members and nonmembers is misleading.

Particularly is this true as regards the year 1923. The finding shows that 98.30% of the loans made in that year were made to members. This is because—

(*a*) It ignores loans made to other building and loan associations, and financial institutions and

mortgages purchased. Including these items in nonmember loans will show such loans to amount to 25% instead of 1.70%.

(*b*) It accredits to members the full amount of the loan although that amount is far in excess of the members' subscription to stock. The borrower was a nominal member only and was not a member in the sense of sharing in accordance with his weekly deposits. This it is submitted is not a compliance with the spirit of the Revenue Act of 1921. (But see *Acklin* v. *People's Savings Association*, 293 Fed. 392; Sol. Mem. 1469, III–1 C. B. 252; Sol. Mem. 2133, III–2 C. B. 218; Sol. Mem. 2116, III–2 C. B. 209.)

The motion to remand

A motion to remand to the Court of Claims for additional findings of fact and brief in support thereof has heretofore been filed in this case by the Government. While it is believed that, upon the facts already found by the Court of Claims, the decision by the Court of Claims is erroneous and should be reversed, it is further believed that the facts requested in the motion to remand strongly indicate that the respondent herein was not a building and loan association in fact, and continued merely to be such in name, and that it was entirely outside not only the spirit and intent but also the letter of the exemption from income taxes. The importance, materiality, and effect of the findings requested in the motion to remand are more

fully set out and discussed in such motion and brief in support thereof, to which the Court's attention at this time is respectfully called, without needless repetition thereof. The most important additional finding requested is that, in a colorable attempt to comply with the requirement of the Revenue Act of 1921 that the business should be confined to making loans to members, the respondent issued nominal amounts of stock to persons to whom loans were made.

CONCLUSION

For the reasons heretofore set forth it is respectfully submitted that the decision by the Court of Claims is in error and should be reversed. And, while it is believed that upon the facts already contained in the findings of the Court of Claims such reversal should be made, it is further submitted that if this Court can not reverse the decision upon the findings already made the motion to remand should be granted upon the additional findings requested, which, it is believed, make reversal of such decision imperative.

Respectfully submitted.

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SEPTEMBER, 1928.

APPENDIX

Regulations 33, Art. 87 (applicable to 1913 Act), provides:

> The act specifically enumerates and exempts from its provisions and requirements labor, agricultural, or horticultural organizations, mutual savings banks not having a capital stock represented by shares, fraternal beneficiary societies, orders, or associations operating under the lodge system, or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, and providing for the payment of life, sick, accident, and other benefits to the members of such societies, orders, or associations, and dependents of such members, domestic building and loan associations, cemetery companies organized and operated exclusively for the mutual benefit of their members, any and all corporations or associations organized and operated exclusively for religious, charitable, scientific, or educational purposes, no part of whose net income inures to the benefit of any private stockholder or individual, business leagues, chambers of commerce, or boards of trade not organized for profit, no part of the net income of which inures to the benefit of the private stockholder or individual, and civic leagues or

similar organizations not organized for profit, but operated exclusively for the promotion of social welfare.

Domestic building and loan associations are among those enumerated as exempt from the requirements of the law. A domestic building and loan association is held to be one organized under and pursuant to the laws of the United States, or of a State or Territory thereof, or under the laws applicable to Alaska or the District of Columbia. Mutuality in operation and in the distribution of profits and benefits is essential to exemption. Therefore, in order to come within the exempted class such associations must not only be "Domestic," as defined, but they must be organized and operated exclusively for the mutual benefit of the members; that is, all the profits and benefits provided for in the articles of association and by-laws must be ratably distributed among all members regardless of the kind of stock held, according to the amount of money they have on deposit. An association issuing different classes of stock upon which different rates of interest or dividends are guaranteed or paid, does not come within the exempted class.

Regulations 33 (Revised), Art. 68, Paragraphs 313, 314, and 317 (applicable to 1916 and 1917 Acts), provides:

PAR. 313. *Unconditional.*—Among the corporations exempt from the tax, without condition, are labor, agricultural and horticultural organizations, mutual savings bank

not having capital stock represented by shares, fraternal beneficiary society, order, or association operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, domestic building and loan associations, Federal land banks, and national farm loan associations, organized pursuant to the Act of July 17, 1916, joint-stock land banks as to income specified in the law, and public utilities whose income inures to the benefit of any State, Territory, or political subdivision thereof.

PAR. 314. In all cases wherein the exemption is without condition, and the collector is satisfied that the organization comes within the exempted class, he will be authorized to eliminate it from his list and relieve it from the necessity of making returns.

PAR. 315. Corporations exempt under the Act of September 8, 1916, are also exempt from the war income tax imposed by Title I of the Act of October 3, 1917.

Art. 70 of said Regulations 33 (Revised) provides:

Domestic building and loan associations.—A domestic building and loan association entitled to exemption is one organized under and pursuant to the laws of the United States or under and pursuant to the laws of some State or Territory thereof, and which is actually carrying on for the benefit of its members a building and loan association business in accordance with the laws under

which it is organized. The fact that such an association issues fully paid or prepaid shares, calling for a specified rate of interest or dividends, will not disqualify it for exemption. The exemption is without qualification other than that the association is a domestic building and loan association. If a corporation by any other name is carrying on an exclusive building-and-loan business, before it is entitled to exemption it will be incumbent upon it to show to the satisfaction of the commissioner of internal revenue that it is in fact a building and loan association.

Art. 515, Regulations 45 (1920 ed.) (applicable to 1918 Act), provides:

Building and loan associations and cooperative banks.—In general, a building and loan association entitled to exemption is one organized pursuant to the laws of the United States or of some State or Territory thereof, which accumulates funds to be loaned to its members and to be repaid in small periodical installments, and in which the members of the association share in the profits on substantially the same footing. It does not prevent exemption that the association issues prepaid stock entitled to a specified percentage of the profits. Where a building and loan association has no other features which render it liable to income tax, it will ordinarily not be subject to tax merely because—

(1) It has paid-up shares which are (a) preferred as to earnings, and (b) have a definite rate of interest which may be higher

than the rate of dividends paid on other stock, or

(2) Its balance sheets show that it is lending considerable sums to nonmembers, or

(3) It is a regular borrower of large sums of money which it uses for loans to members, the dues paid by members being entirely inadequate for the business transacted by it.

Cooperative banks without capital stock organized and operating for mutual purposes and without profit are exempt. Credit unions, such as those organized under the laws of Massachusetts, being in substance and in fact the same as cooperative banks, are likewise exempt from tax.

Art. 515, Regulations 45 (1920 ed.), T. D. 3179, June 16, 1921 (applicable to 1918 Act), provides:

Building and loan associations and cooperative banks.—In general, a building and loan association entitled to exemption is one organized pursuant to the laws of the United States, or some State or Territory thereof, which accumulates funds for the primary business of making loans to its members for the purpose of building or acquiring homes, and in which the members of the association share in the profits on substantially the same footing. It is essential that the association should be (a) mutual; (b) organized and operated for the accumulation of funds to be loaned primarily to members for home building. Where a building and loan association has no other features which render it liable to income tax it will ordinarily not be subject to tax merely because—

(1) It has paid-up shares which are (a) preferred as to earnings and (b) have a definite rate of interest which may be higher than the rates of dividends paid on their stock.

(2) It borrows large sums of money (accepting deposits is considered as borrowing), which it uses primarily for loans to members, the dues paid by members being entirely inadequate for this purpose.

(3) In times of small demand it loans considerable sums to nonmembers from or invests association funds which would otherwise lie idle and unproductive.

(4) The amount of prepaid or full-paid stock is disproportionate to running or installment stock, provided the issuance of such prepaid or full-paid stock is incidental to the furtherance of the main business of the association; that is, that it is intended to provide a fund from which loans may be made primarily to persons subscribing to the running or installment stock to enable them to acquire or build homes.

Where, however, the facts show that a building and loan association is borrowing large sums of money from nonmembers with no reference to the borrowing needs of its members, and is in turn loaning these sums to nonmembers, the number of depositors being disproportionate to the number of members, and the amounts loaned to nonmembers being disproportionate to the amount loaned to members, such association will be deemed to be taxable and will be granted exemption

only upon a satisfactory showing to the Commissioner that it is, in fact, a bona fide building and loan association within the meaning of this article.

Cooperative banks without capital stock organized and operated for mutual purposes and without profit are exempt. Credit unions, such as those organized under the laws of Massachusetts, are in substance the same as cooperative banks, and when organized and operated without capital stock, for mutual purposes and without profit, are likewise exempt.

Art. 515, Regulations 62 (applicable to 1921 Act), provides:

Building and loan associations and cooperative banks.—In general, a building and loan association entitled to exemption is one organized pursuant to the laws of any State, Territory, or the District of Columbia, which accumulates funds to be loaned primarily to its shareholders for the purpose of building or acquiring homes. In order to be exempt the association (1) must be mutual, that is, all of its stockholders or members must share in the profits on substantially the same footing; and (2) must be operated so that substantially all of its business is confined to the making of loans to bona fide shareholders. A building and loan association otherwise exempt does not lose its exempt status because—

(1) It has paid-up shares which are (a) preferred as to earnings, and (b) have a defi-

nite rate of interest which may be higher than the rate of dividends paid on other stock.

(2) It borrows money (accepting deposits is held to be a form of borrowing) which it uses for loans to shareholders, the dues, fines, and penalties paid by shareholders being inadequate for this purpose.

(3) It makes loans to nonmembers from accumulated funds which are not needed for loans to shareholders. In any such case, however, the burden will be upon the association to show that substantially all of its loans are made to members.

(4) The amount of its prepaid or full-paid stock is disproportionate to running or installment stock, provided the issuance of such prepaid or full-paid stock is ancillary to the furtherance of the main business of the association; that is, that it is intended to provide a fund from which loans may be made primarily to persons subscribing to running or installment stock to enable them to acquire or build homes.

Cooperative banks without capital stock organized and operated for mutual purposes and without profit are exempt. Credit unions such as those organized under the laws of Massachusetts, being in substance and in fact the same as cooperative banks, are likewise exempt from tax.

See also Sec. 213 (b) (10), Revenue Act of 1921, exempting dividends and interest paid to members, and Art. 89, Regulations 62.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1927.

No. 700

THE UNITED STATES, PETITIONER,

vs.

THE CAMBRIDGE LOAN & BUILDING COMPANY.

BRIEF OF RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

The jurisdiction of this Court, the issues and the statutes involved are correctly set forth in the petitioner's brief.

Statement.

The respondent brought suit in the Court of Claims to recover income taxes it was required to pay simultaneously for the several years 1918 to 1923, inclusive, contending that it was, during the years 1918, 1919,

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CLERK

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1927.

No. [redacted] 46

THE UNITED STATES, PETITIONER,

vs.

THE CAMBRIDGE LOAN & BUILDING COMPANY.

BRIEF OF RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

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1920, and until November 23, 1921, the date of the passage of the Revenue Act of 1921, a domestic building and loan association within the purview and meaning of the Revenue Act of 1918, which was in force during that entire period; and it contended that, subsequent to November 23, 1921, for the years 1922 and 1923, which are controlled by the provisions of the Revenue Act of 1921, it was a domestic building and loan association, substantially all of whose business was confined to making loans to its members.

There are thus two separate acts of Congress to be interpreted. Respondent claims that under both these acts it was exempt from the payment of income taxes. The Government contends that the respondent was not a domestic building and loan association during any of these years.

The respondent has been engaged exclusively in the business of a building and loan association in the State of Ohio for the past forty-two years, without interruption, and has regularly since the creation of the office of the Superintendent of Building and Loan Associations in the State of Ohio, in the year 1891, filed its reports annually and was annually inspected by that officer, and at all times found to be complying with all the laws of the State of Ohio in respect of the carrying on of the business of a building and loan association. Not until September 18, 1924, did the Commissioner of Internal Revenue attempt to assess against the respondent income taxes and on that date he made assessment of income taxes against respondent retrospectively for each of the years 1918 to 1923, inclusive.

The facts are very fully and clearly set forth in the findings of fact of the Court of Claims, which include every material fact necessary to determination of this case. There has been some complaint of these facts in the petitioner's brief; however, it will presently be seen that the minor objections of petitioner in respect of the findings of fact by the Court of Claims are unimportant and do not affect the real issues involved.

The only questions in this case involve statutory interpretation and may be briefly stated thus: In respect of the Revenue Act of 1918, which governs the right of respondent to exemption during several of the years under consideration, did Congress intend to exempt from income taxes *bona fide* building and loan associations organized and operated under and in conformity with the laws of the several States? by virtue of which, alone, they exist; and in respect of the 1921 Act, did Congress intend that these same building and loan associations shall be exempt from income tax provided after the passage of that act they confined their business substantially to making loans only to their members? The respondent contends that this was the intention of Congress, and the Court of Claims has sustained its contention. The Government claims that under these two statutes the Commissioner of Internal Revenue was delegated with authority by Congress to determine, and that succeeding Commissioners of Internal Revenue should have the right to determine, in accordance with their own individual conceptions or caprices, whether a building and loan association organized, created and doing business in good faith, in

conformity with the only laws which define and permit its existence, is not a building and loan association. The issues thus raised are sharp and well defined and require only the application of the rules of statutory interpretation for their solution.

ARGUMENT.

This Court has aptly observed that "a page of history is worth a volume of logic" in construing the terms of a statute, and has laid down accordingly the following cardinal principles:

(1) Courts must take notice of the history of legislation, and, of different possible constructions, select and apply the one that best comports with the genius of our institutions, and therefore most likely to have been the construction intended by the law-making power (Texas & P. R. Co. vs. Interstate Commerce Commission, 162 U. S., 197).

(2) In construing a statute, courts may recur to the history of the times when it was passed in order to ascertain the reason for its passage, as well as the meaning of its provisions (Platt vs. Union P. R. Co., 99 U. S., 48; U. S. vs. Union P. R. Co., 91 U. S., 72).

(3) Where the language of the statute is in any manner ambiguous, or the meaning doubtful, resort may be had to the surrounding circumstances, the history of the times and the defect or mischief which the statute was intended to remedy (Smith vs. Townsend, 148 U. S., 490).

In order to determine whether the Court of Claims has grossly erred in its interpretation of these statutes and accordingly the propriety or necessity of reviewing its judgment, it should only be necessary to consider, in conjunction with the language of the statutes, the history of the legislation relating to the exemption of these associations up to the time of the passage of the Revenue Acts of 1918 and 1921, and the executive construction and judicial interpretation of prior statutes in *pari materia*.

History of the Legislation, the Previous Statutes in Pari Materia and the Executive Construction and Judicial Interpretation Thereof.

The present system of taxation can be said to have had its inception with the passage of the Act of 1909, since which there have been successively enacted the Act of 1913, the Act of 1916, the Act of 1918 and the Act of 1921, all relating specifically to the identical subject matter now under consideration.

The Act of August 5, 1909 (36 Stat. L., 113-118), provides at Section 38:

> "That nothing in this section contained shall apply * * * to domestic building and loan associations *organized and operated exclusively for the benefit of their members*, * * *" (Italic letters supplied.)

Under the provisions of this act a large number of building and loan associations in Ohio were taxed, resulting in the institution of several suits,

namely, Park View Building & Loan Association *v.* Herold, 203 Fed., 876; Herold *v.* Park View Building & Loan Association, 210 Fed., 577; Bellefontaine Building & Loan Co. *v.* McMaken, 216 Fed., 526; Central Building, Loan & Savings Co. *v.* Bowland, 216 Fed., 526. Under all of these decisions interpreting the provisions of the 1909 Act, which restricted exemption of domestic building and loan associations to those which were *organized and operated exclusively for the mutual benefit of their members*, every decision was in favor of exemption of the building and loan associations, it being held that the making of loans to nonmembers and the accepting of deposits from them (for which they were taxed) did not affect the mutuality of the members, since no nonmember and no depositor who was not a member received any of the earnings of the association, which were exclusively divided among the members.

The next legislation was the Act of October 3, 1913 (38 Stat. L., 144, 172), wherein it was provided:

> "(G (a)) Provided, however, that nothing in this section shall apply to labor, agricultural, or horticultural organizations, or to mutual savings banks not having a capital stock represented by shares, or to fraternal beneficiary societies, orders, or associations operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, and providing for the payment of life, sick, accident, and other benefits to the members of such society, orders, or associations and dependents of such members, *nor to domes-*

tic building and loan associations, nor to cemetery companies, organized and operated exclusively for the mutual benefit of their members, nor to any corporation or association organized and operated exclusively for religious, charitable, scientific, or educational purposes, no part of the net income of which inures to the benefit of any private stockholder or individual, nor to business leagues, nor to chambers of commerce or boards of trade, not organized for profit, or no part of the net income of which inures to the benefit of the private stockholder or individual; nor to any civic league or organization not organized for profit, but operated exclusively for the promotion of social welfare." (Italic letters supplied.)

When the 1913 Act was introduced in the House of Representatives the exact language of the 1909 Act was incorporated, restricting exemption as before to associations *organized and operated exclusively for the mutual benefit of their members*. (H. R. 3321, Apr. 1, 1913; Sec. II (G1)). On May 8, 1913, the day the bill was passed by the House, the restricting clause was deliberately stricken out, and as stricken out the bill was passed by the Senate, so that the act provided that nothing therein should apply to "domestic building and loan associations."

No building and loan associations were required to file returns under this act, which was in force until September 8, 1916, when the Revenue Act of 1916 was passed, and no taxes were assessed or collected thereunder.

The next legislation was the Revenue Act of September 8, 1916 (39 Stat., 766), wherein it was provided:

> "SECTION II (*a*) That there shall not be taxed under this Title any income received by any—
> "(4) *Domestic building and loan associations* and cooperative banks without capital stock organized and operated for mutual purposes and without profit." (Italic letters supplied.)

The 1916 Act began with the introduction of H. R. 16763, 64th Cong., 1st Session, wherein at Section XI (*a*) provision was made for the exemption of "domestic building and loan associations," being a re-enactment of the 1913 Act. After the bill reached the Senate an amendment was proposed known as Amendment No. 65 (see Conf. Rep., p. 29). There we find the following statement in the report of the conferees of the Senate and House:

> "The Senate amendment provides that the income of *co-operative banks organized and operated for mutual purposes and without benefit* shall be exempted from the income tax provision. The House recedes from its disagreement to the Senate amendment with an amendment exempting *co-operative banks without capital stock organization and operated for mutual purposes and without profit.*" (See Book No. H. H. J. 2379, A. 4, 1916, Congressional Library.)

No effort, as stated, was made to subject any building and loan association to income taxes under the 1913 Act at any time, and no effort was made to sub-

ject building and loan associations to income taxes under the 1916 Act, which was in force until February 24, 1919, when the Revenue Act of 1918 was passed. The Act of October 3, 1917, made no change in respect of exemption of building and loan associations but merely increased the rates of income taxes of individuals and corporations subject to the tax, as well as the rates of Federal estate taxes.

After Congress had passed the 1916 Act in September of that year we find that on February 26, 1917, Congress passed a special act (Chap. 129) which directed the Secretary of the Treasury to pay to the several building and loan associations therein named the sums set forth therein, the same to be a refund of taxes "*illegally collected* from said associations under the *Excise Tax Act of August 5, 1909.*" This act was to enable all associations from whom taxes had been exacted under the early 1909 Act, where the statute of limitations had tolled against refund claims, to recover all such taxes. All other associations against whom such taxes had been collected had already received refunds as a result of the court decisions referred to. Regulations promulgated by the Commissioner of Internal Revenue and approved by the Secretary of the Treasury under the 1916 Act, at all times that it was in force, provided, at Article 68, Reg. 33, that building and loan associations organized and operated under the laws of any of the States of the United States are exempt under the provisions of Section 11 (*a*) of the Revenue Act of 1916.

Article 68 of Regulations 33, promulgated under the 1916 Act, relating to exemption, is headed "Unconditional," and states as follows:

> "Among the corporations exempt from the tax, without condition, are * * * domestic building and loan associations * * *."

The foregoing is the history of the legislation and of the judicial interpretation and executive construction thereof at the time the Congress on February 24, 1919, passed the Revenue Act of 1918, re-enacting without change the provisions of the 1916 Act relating to the exemption of these associations.

The Revenue Act of 1918 (40 Stat., 1073) provided:

> "SECTION 231. That the following organizations shall be exempt from taxation under this Title:
>
> "(4) *Domestic building and loan associations* and co-operative banks without capital stock organized and operated for mutual purposes and without profit."

No returns were filed by and no taxes assessed against building and loan associations under this act so long as it was in effect, it having been superseded by the Revenue Act of 1921, enacted November 23, 1921.

And now, so it is that the Commissioner of Internal Revenue in retrospectively assessing in the year 1924 taxes against respondent for the years prior to the passage of the 1921 Act, namely, for the years 1918 to

1921, pretends that the Congress did not intend to exempt these associations under the provisions of the 1909 Act or the 1913 Act or the 1916 Act, or the 1918 Act; that the successive re-enactment of this exemption provision over a period of 12 years was not intended as an adoption of the previous executive construction and judicial interpretation of prior acts; that he is not in any manner bound thereby; and that what the Congress intended and meant all along was to exempt only such associations as might come within the exemption provisions of the 1921 Act subsequently enacted and necessarily not theretofore in existence. Surely he is not aware of the oft-repeated ruling of this Court that the meaning of a particular statute should be determined in the light of prior acts in *pari materia* that have been interpreted and construed (U. S. *v.* Saunders, 22 Wall., 492; U. S. *v.* Farden, 99 U. S., 10; Vane *v.* Newcombe, 132 U. S., 220; U. S. *v.* Central P. R. Co., 118 U. S., 235; The Aurora *v.* U. S., 70 Cranch, 382).

Clearly, the 1918 Act and its predecessors are dead issues and cannot be revived at this late date by an attempt of the Internal Revenue Commissioner to place an interpretation thereon directly contrary to the intention of Congress, which has repeatedly re-enacted this statute in the light of prior executive construction and judicial interpretation of statutes in *pari materia*.

This brings us to the 1921 Act, but, before passing on, it may be well to refer to the eminent authority, Judge Endlich, whose reasoning in his work on Building and Loan Associations is in true accord with the

decisions of the Federal courts, *supra*, interpreting the stringent provisions of the 1969 Act. We find at Section 313 of this work, written in 1882, the following:

> "It is said in Pennsylvania, and in Ohio, and seems to be the understanding of the law in Indiana, in Kansas, and in Massachusetts, that a building association has the power of lending its money to members only, and not to strangers. *It must be admitted that there is nothing in the reason or constitution of building associations to favor of the doctrine. On the contrary, although it undoubtedly was their design that eventually all the members should become borrowers, in practice there is always a large portion of them who content themselves with paying, and never think of drawing out. Thus, if none but members may receive loans, the funds of the society may go begging; it may be subjected to constant losses on account of their lying idle; and the very end aimed at by the association, the speedy and profitable winding up, be delayed by a restraint as unreasonable as the license is harmless. Yet, in the absence of special statutory authority giving that license, the doctrine denying it to building associations must be held to be established by authority.*" (Italic letters supplied.)

Singular it is, the author refers to the fact that at the time of writing (1882) the State of Ohio and five other States did not permit these things, but the author states that whether or not an association may engage in this further activity *depends upon the State statute*. However, as early as 1908, the State of Ohio by legis-

lative enactment specifically authorized these associations to accept deposits from and make loans to non-members, and it is still the law. (See Ohio statute cited in the opinion of the Court of Claims, Rec., 10.) All modern authors writing on the subject are in accord with Judge Endlich.

The 1921 Act.

But, on November 23, 1921, Congress decided to no longer exempt these associations as they existed unless thereafter they confine their loans substantially to their members. Thus, when the 1921 Act was passed, Congress then decided to exempt the same associations which had been exempted from tax under every prior income-tax law, but placed one restriction upon that exemption, and that restriction was that these associations, to be exempt in the future, must confine their business to making loans to members. In all other particulars and in all other respects Congress adopted the interpretation of the previous acts. It did not see fit to place any further restrictions upon them, such as prohibiting them from accepting deposits or requiring borrowers to subscribe to stock to the full amount of the loans, or to direct how they shall operate or conduct their business, or to in any way interfere with the common practice existing among the associations in the various States other than in respect of the persons to whom they may make loans. The interpretation, therefore, of the 1921 Act becomes rather simple and requires only a practical determination of the extent to which these associations, after the

passage of the 1921 Act, may indulge in making loans to nonmembers if they would retain their right to exemption.

The Court of Claims has held that respondent, subsequent to the passage of the 1921 Act, has substantially complied with its provisions. Has it committed gross error? Is its judgment unsound or its conclusions illogical? If not, its decision needs no review.

There are only two years (1922 and 1923) involved herein which are controlled by the provisions of the 1921 Act. Bearing in mind that this act was only five weeks before the year 1922, and that its numerous provisions are not at once broadcast among the people of the cities, towns, and hamlets of the country, let us see what the facts are as found by the court.

During the year 1922 the record shows (p. 10) that the respondent made 225 separate loans, of which 180 of them were to its members in the aggregate amount of $209,960.35, and it made 45 loans to those who were not members in the aggregate amount of $113,530. In respect of the number of loans made, 80 per cent of them were to members and 20 per cent to those who were not members. In respect of the amount of money loaned, 70 per cent of it was loaned to members and 30 per cent to nonmembers. It should be noted, however, in Finding IX (Rec., 11), that at no time did the respondent lend money to a nonmember in preference to a member, and therefore, if it had a pre-existing surplus of funds on hand, the amount of so called loans to others than members constituted little more than an investment of such surplus funds, which investment

only accrued for the benefit of the members, who alone received dividends on the earnings of the association. Petitioner contends that too large an *amount of money* was loaned to nonmembers during this one year, but the amount of money is not the only consideration necessary to determine the ultimate question of fact. Surely, if the association had made one loan to a member in the amount of $250,000, and 100 loans to persons who were not members, in the aggregate amount of $20,000, it would scarcely be correct to say that thus, because 93 per cent of the *money* which it loaned was to a member of the association, it confined its business substantially to making loans to its members, since 99 per cent of the loans which it made were to nonmembers. The question simply involves a practical consideration, bearing in mind the circumstances and necessities of the association upon the advent of the new act, and if it has not grossly overstepped the bounds of a practical interpretation of the statute, it should not be denied exemption for this one year. It seems clear that respondent has quite substantially complied with the statute.

The word "substantially," used in the 1921 Act in respect of the making of loans to members, has been defined in "Words and Phrases, 2d Series, Vol. 4, page 753," as follows:

> "'Substantially' means in substance; in the main; essential; by including the material or essential part. See Town of Checotah *v.s.* Town of Eufala, 110 Pac., 1014, 1019; Vannest *v.s.* Murphy, 112 N. W., 236, 238; 135 Iowa, 123. See also Electric Candy Machine Co. *v.s.* Morris, 156

Fed., 972, 974; Eisfeld *vs.* Kenworth, 50 Iowa, 389, 390."

In the case of South Penn Oil Co. *vs.* Knox, 69 S. E., 1020, 1021; 68 W. Va., 362, there was involved an oil and gas lease, describing the premises as being all that certain tract of land situated in a certain district of the waters of a designated stream bounded "substantially" as follows, etc. The court held that the word "substantially" there was intended to mean "about" or "in the main," as designated, and not "wholly" or "completely."

Surely, since 80 per cent of all of its loans was to members and 70 per cent of all its money loaned was to members, there was a substantial compliance with the exemption provision.

Let us now see what were the facts, as found by the court for the year 1923.

During the year 1923 (Finding VIII, Rec., 10) there were 301 separate loans made, of which 272 were to members in the aggregate amount of $69,111.98 and 29 loans were made to others than members in the aggregate amount of $10,545. Thus, in respect of the number of loans made, 90 per cent of them were to members, and in respect of the amount of *money* loaned during the year *more than 86 per cent* was to members.

A review of the record of the facts in this case shows beyond any question of doubt that the respondent, which had been doing business as a building and loan association for forty-five years, was in fact and in truth a *bona fide* domestic building and loan association and has substantially complied with the provisions of law in respect of its exemption during the en-

tire period involved. There seems to be nothing to construe and no error to review.

It is now only necessary to briefly advert to a few statements contained in the petition and the brief of petitioner respecting the amount of money involved and some minor complaints regarding the findings of fact made by the court below and a few observations concerning the reasons assigned by petitioner to support the granting of the writ in this case.

The Amount Involved.

Although it is not to be found in the record of this case, petitioner has informed this Court that if the judgment of the Court of Claims is allowed to stand, the Government may have to refund approximately $2,500,000 of taxes which it deliberately collected retrospectively going back over a period of nearly ten years from the present date and nearly twelve years since the passage of the Revenue Act of 1916. Petitioner states that there are about 1,300 associations which have not yet been exempted, but does not state from how many of these taxes have been collected retrospectively. A stipulation was filed in the court below at the request of the Government wherein it appeared that there were 11,369 building and loan associations in the United States, of which 10,060 have been exempted by the Commissioner of Internal Revenue.

If the total amount which has been collected covering the alleged liability since 1918 (a period of nearly ten years), has been $2,500,000, it indicates that the annual taxes of all kinds collected from building and loan associations throughout the United States have

amounted to $250,000. It is not only doubtful but certain that Congress has not seen fit to adopt a taxing measure which would produce no more revenue for the support of the Government than $250,000 a year. There is not a single item involved in any of the taxing acts designed to produce a revenue so small as this.

The record thus called to the attention of this Court at the instance of the petitioner seems to be a complete justification of the wisdom of Congress in exempting these associations as they existed in this country in the various States. The exemption, of course, is the exemption of a class of institutions. It confirms the judgment of Congress in assuming that the various States were as much, if not more, interested in preserving and perpetuating the integrity and worthiness of these local institutions as the Federal Government could possibly be, and that no mistake would be made in thus exempting them from taxation. The record proves nothing else.

This Court, of course, has not been informed of the basis upon which the amount involved has been either assessed or collected and it is interesting, if not curious, to note the basis upon which the Internal Revenue Bureau has considered exemption of some of these associations against whom it has either assessed or collected these taxes.

In Cumulative Bulletin III 2, at page 260, the Commissioner states that an association which accepts deposits from nonmembers and makes loans to nominal shareholders is entitled to exemption from taxation when the rate of interest it charges to borrowing members is not exceeded by the rate of dividends paid

to non-borrowing shareholders and it compares favorably with and only slightly exceeds the rate of interest paid to depositors.

In a very recent case, Cumulative Bulletin V-1, at page 291, the Commissioner states that an association which does not inquire and make certain the use to which the borrowing member intends to devote the money loaned to him is not entitled to exemption and that the positive statement by the association that 95 per cent of its loans were for the purpose of acquiring homes is not to be considered. In other words, the association must absolutely know that the loan it has made to its member which it has no power to control is going to be used for the purpose of building a home. This is beyond the requirement laid down by any textbook writer or any court in the United States.

From the foregoing rulings made by the Department it is impossible to determine the basis of either the exemption or nonexemption of the various associations which may be included within this gross statement reflecting the beneficence of the Department in the granting of exemptions. It is obvious, however, that none of them has been given the benefit of the slightest doubt under the strict legislative interpretation of the Treasury Department.

These rulings were clearly in derogation of the provisions of the statute; are purely legislative in character; and directly contrary to the established law as laid down by all modern authors on building and loan associations.

In 9 C. J., 954, Sec. 70, we find it stated that a building and loan association, unless restricted by statute,

may lend its money for other purposes than building purposes, and it is not required to ascertain the use to which a borrowing member intends to apply the money.

In Sundheim on Building & Loan Associations, 2d Ed., page 20, it is stated that a building and loan association may lend its money for the purchase of real estate or for any lawful purpose or business. As far back as 1859, in the case of Juniata Building & Loan Association *vs.* Mixwell, 84 Pa., 313, it was held that a building association need not inquire for what purpose a loan is obtained or what use will be made of the money.

On page 22 of the work above cited we find the following:

> "The borrower may, if he so desire, build a house with the money advanced, or he may use it in any trade or business. The association merely loans or advances the money and the use to which it is put is none of its concern."

On page 24 of the same work the author speaks of these associations as follows:

> "They have grown to such an extent in recent years that they no longer restrict their money to the home buyer, but loan their money to the mere investor or dealer in real estate. They are the holders of large mortgages secured upon farms, factories and other business property and rows of stores and dwellings. This is not an abuse of their powers or a departure from their main purpose, but of course a natural and proper expansion along healthy and legitimate lines. All legislation in recent years has been to enlarge

and broaden their powers, not to confine and restrict them. The courts have been liberal in the construction of these especially delegated powers, and as the result they have grown and changed as conditions required."

Again, on page 112, Sec. 111, the same author states:

"Loans are made for the purpose of purchasing a homestead or other real estate, or for any lawful purpose or business, but there is no duty or obligation of the association to inquire for what purpose the loan is obtained or to require any stipulation from the borrower as to what use he will make of the money, or in any manner to supervise or control its disbursement."

Considering the manner in which it was done and the fact that it includes not only income taxes collected but capital stock taxes as well, what has the amount involved to do with this case?

Petitioner's Objections to the Court's Findings.

Petitioner criticizes the Court of Claims for not including in the category of loans made to non members during the years controlled by the 1918 Act the small amount of first mortgages on real estate purchased by respondent out of its funds for the benefit of its members. These mortgages were not loans which this association made and for which a mortgage was given to it. The loan was made by some other institution or some individual and the mortgage given to him. The security being first class and the interest a good investment, the association simply purchased that mortgage from the mortgagee who assigned it to the asso-

ciation. It would indeed be anomalous to call that a loan made by the association. Petitioner only desired to include these mortgages in an effort to swell the percentage of loans, and its request was fairly excluded.

Petitioner complains that the court below did not find, in respect of the years covered by the 1918 Act, the number of depositors as compared with the number of stockholders. Such a finding is wholly immaterial and has nothing to do with the issue.

Petitioner also complains that the court declined to consider as a loan to a non-member, money which the respondent deposited in other building and loan associations at interest for the benefit of its members. Likewise we say it would be anomalous to treat as a loan made in the ordinary course of business a sum of money which one has deposited to his own credit in some institution. The criticism is frivolous. In Finding VII (Rec., 9) there is set forth as Item 10 of the assets the amounts deposited in other building associations during each of the years in question; and what do they amount to? Not in one year do they equal as much as 2 per cent of the assets of the association. Moreover, it has nothing to do with the matter of exemption.

Finally, petitioner complains that the court below has failed to make other findings of fact which would fortify the position of the Government. In no instance, either in the petition or in the brief, has there been indicated how any of these matters complained of could in the slightest possible degree affect the issue involved and no attempt has been made to show how it affects the interpretation of the statute.

The paraphrasing of percentages contained in petitioner's brief, on pages 5 and 6, results from a set-up which is not in accordance with any of the facts in the case, either as found by the court or as contained in the record anywhere. As far as they concern the issues involved, they seem to be meaningless and only serve to perhaps "muddy the water."

Reference is made on page 8 of petitioner's brief to three cases to support his contention that a Federal tax law may not be abridged by force of a local statute. There is no such issue in this case. The merest glance at the cases cited indicates their irrelevancy.

Reference is also made to the case of Eversmann *vs.* Schmitt, 53 Ohio State, 174, in respect of what constitutes a building and loan association, bearing particularly upon the matter of making loans. This case was decided in the Ohio court in 1892, at a time when under the State law these associations were not permitted to make loans or accept deposits from non members. As hereinabove stated, this law was changed in 1908, prior to the passage of any of these revenue acts, and ever since such loans and deposits have been specifically authorized. The decision, therefore, is not authority in that State subsequent to the year 1908.

On page 9 there is also cited Lilley Building & Loan Company *vs.* Miller, 280 Fed., 143, involving the 1918 Act. A glance at that case shows, not only that the decision was unsound as found by the Court of Claims, but that it involved a situation wherein the facts were quite eccentric. Only four-tenths of one per cent of its loans were made to members being the outstanding feature. The court held that that associa-

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THE CAMBRIDGE LOAN & BUILDING COMPANY.

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

RESPONDENT'S REPLY IN OPPOSITION TO PETITIONER'S MOTION TO REMAND, AND BRIEF IN SUPPORT THEREOF.

L. L. HAMBY,
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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1928.

No. 46

THE UNITED STATES, PETITIONER,

vs.

THE CAMBRIDGE LOAN & BUILDING COMPANY.

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

RESPONDENT'S REPLY IN OPPOSITION TO PETITIONER'S MOTION TO REMAND, AND BRIEF IN SUPPORT THEREOF.

The Government's motion is to remand this case to the Court of Claims for the purpose of having found certain alleged additional facts set forth specifically in five separate paragraphs on pages three and four

of its motion, it being represented that these facts are material and necessary for a determination of the issue and that they were not found by the court below although it was requested to find them.

It is with great reluctance that we feel constrained to demonstrate the motion as a purely frivolous one for the reason that all of the alleged additional *facts* sought by the motion, with one wholly immaterial exception, have actually been found and are now before this Court. We cannot conceive any other purpose of the motion except to delay the final judicial determination of a case which is of the utmost importance to the building and loan associations of the State of Ohio and its millions of members against which the Internal Revenue Bureau has primarily leveled its interpretation of the exemption provisions of the Revenue Acts involved.

This case has been pending for four years and it will be seen from the record that after the judgment was entered by the Court of Claims the Government waited until the very last day to file a motion for a new trial. When this was overruled it waited until the very last day to file a petition to this Court for a writ of certiorari and although that was granted on April 2nd it has waited for six months to file this motion to remand, which, if granted, would send the entire case back to the Court of Claims and the question of vital importance both to the Government and to the public would be thus postponed for perhaps another year.

It is important to bear in mind that the attempt in this case, as in all other cases, is to assess retroactively for a period of five years taxes against these associations for which they had not been required to file any returns and during which under the Department's own regulations they had a right to suppose that they were exempt from this tax. To be now required to pay taxes for all of those back years after they have already paid all of their earnings in dividends to their members to aid them in the building of their own homes, which is the primary reason for their exemption by Congress, would require many of them to liquidate. More than this, all of the millions of members in the years past were required to pay income taxes on all dividends they received from building and loan associations because dividends are subject to the normal income tax if the corporation is exempt from taxation and therefore does not pay a normal tax at the source. It will be readily seen, therefore, that if these associations are now required retrospectively to pay these back taxes for ten years everyone of the millions of members who have paid the normal tax to the Government will automatically have paid a tax which was not due and which would, therefore, have been illegally collected; but they would now be powerless to recover from the Government a single dollar thereof because the statute of limitations has run against the filing of any claim for refund. This statute of limitations is daily running against hundreds and thousands of such potential claims if this Court should hold that building and loan associations of this character are subject to

the tax. It will thus be seen that it is of the greatest public importance that they have a judicial determination of the issues involved in this case at the earliest possible date.

Now let us demonstrate that the alleged additional findings sought by this motion have already been found by the Court of Claims and in most instances far more in detail than is contemplated by the motion.

We assume that before such a motion would be entertained it must be made to appear (1) that the additional findings requested are questions of fact which appeared competently in the evidence before the court below; (2) that such facts so competently appearing in the evidence were not found by the court below, although it was requested to do so; and (3) that such facts were relevant, material and competent to prove some issue in the case, and without which the issue involved could not properly be determined.

1. The Government contends that the Court of Claims should have found as an additional fact that the dividends paid on running or installment stock steadily decreased, while dividends on paid-up stock steadily increased.

In its finding VII (R., 9) the Court of Claims found as a fact (Item 1 of Liabilities) the amount of running stock and dividends for each of the years involved, showing that they decreased from $219,542.85 in the year 1918 to $152,964.34 in the year 1923, the amount for each year being separately stated. It also found (Item 5 of Liabilities) that the paid-up stock and dividends gradually increased from $45,755.06 in the

year 1918 to $181,248.64 in the year 1923, and the amount for each year intervening is separately stated. It seems, therefore, that whether such facts are relevant, material or competent, or whether they were supported by the evidence, they have been found and are now before this Court for whatever they may be worth.

The Government has failed to cite and cannot cite a single authority of any kind or character whereby a building and loan association may be restricted in the issuance of paid-up or installment stock within the limitation of its charter. The Court of Claims, in its Finding I (R., 8), found that during the years under consideration this association was authorized to issue capital stock not in excess of $1,500,000, and that the par value of each share was $50. The only limitation, therefore, was that at no time could there be outstanding more than $1,500,000 of stock subscribed for, and it makes no difference whether it was being paid for upon the installment plan by the week, by the month, or by the year, or whether it was paid for all at one time, or in any other manner.

2. The Government next contends for additional finding showing that deposits were accepted in large amounts by this association regardless of the borrowing needs of its members for the purpose of realizing pecuniary profit by lending such deposits to non-members. The Court of Claims, in its Finding VII (R., 9), has found (Item 6 of Liabilities) the outstanding deposits for each year under consideration other than deposits or other building and loan associa-

tions, and has also found that during only one year, being the year 1919 (Item 11 of Liabilities), it received deposits from other building and loan associations in the amount of $5,000. The Court of Claims has further found in its Finding VI (R., 9) that the money raised by this association during the years under consideration was principally from payments of stock, from *deposits* by nonmembers and from interest on moneys temporarily deposited by it in bank or loaned to building and loan associations, and the extent of all such transactions was reported to the Superintendent of Building and Loan Associations for the State of Ohio in annual reports. It thus appears that whether or not material, the alleged additional facts here sought have been found. It has also set out in Finding VIII (R., 10) the amount of all loans each year to nonmembers.

It is sufficient, however, to state that the Government is unable to cite a single authority of any kind or character to show that a building and loan association may not accept deposits except only where forbidden to do so by the law of the State or by its charter. Associations in about forty-four of the forty-eight States are permitted to accept deposits. Respondent, however, will be able to show in every case ever decided by a Federal court it is held that acceptance of deposits is clearly and necessarily within the purview of such associations. See Central Building, Loan & Savings Co. *vs.* Rowland, Collector, 216 Fed., 526, 532, 533, 534; Herold *vs.* Park View Building & Loan Association, 210 Fed., 577, 578, 582. See also

Sundheim on the Law of Building & Loan Associations, 2nd Ed., Sec. 9, page 25.

3. The next alleged additional finding which the Government desires is that this association was not concerned with the purpose of the borrower, and did not limit its loans to those to be used for building or acquiring homes, but that it made loans on houses, real estate, farms, business properties, churches, apartment houses, bank stock, industrial stock, municipal and other bonds. The request to have the Court of Claims find that this association was not concerned with the purpose of the borrower is a request for a conclusion to be drawn from facts and may not be required. However, let us see what the court has found. In its Finding III (R., 8), the court found that with the exception of an investment of $5,000 in hotel bonds afterwards disposed of, this association during the entire period under consideration invested its funds in the manner prescribed and permitted under the laws of the State of Ohio for the investment of funds of building and loan associations, reported them annually to the Superintendent of such associations in that State, and received a report each year from that Department upon the conduct of its business. That at least deals with the question of hotel bonds. Now, as to the loans made on farms, churches, business properties and the like, attention is invited to Finding VIII of the Court of Claims (R., 10). There, for each year under consideration, is set forth in detail the number of loans made to members and to nonmembers, the amount of the loans to each and

upon what it was secured, whether upon homes, real estate, farms, business property, churches, or collateral, including bank stock, industrial stock, municipal or otherwise. It seems that this requested finding, like the others, is absolutely frivolous. But, for whatever it may be worth, the facts are already before this Court. The manner in which the Government desires these facts found would be entirely misleading to this Court. It desires the facts found generally instead of specifically as the Court of Claims has already found them. For example, Finding VIII shows that one loan was made to a church in 1919 amounting to $7,500, one in 1920 amounting to $700, one in 1921 amounting to $15,500 and one in 1922 amounting to $5,000, whereas the aggregate amount of all loans made during the period under consideration was $2,200,000.

The Government has failed to cite any authority that holds that a building and loan association may not make a loan to a church or on a farm or on real estate or to acquire homes or for business purposes, but whatever may be the law the facts have been found in detail and these details should not be supplanted by a general finding which would be misleading. This is not the place to discuss the merits of this case.

4. The Government next moves for an alleged additional finding of fact to the effect that this association's loans to members were not confined to borrowers who subscribed to stock equal to the face of the loan, but that the association permitted persons to be

come members upon subscribing in some instances for from one to five shares of stock.

The Court of Claims, in its Finding IV (R., 8), found that under Section I of Article V of this association's constitution it was provided that anyone upon subscribing for or in any manner becoming entitled to or the owner of *any part* of the capital stock of this company shall be deemed a member thereof and a stockholder therein to the extent of the balance of his credits or record on account of said stock. Could anything be clearer than this? One share, or five shares, is a part of the capital stock. The record before this Court, therefore, shows that to become a member of this association it was only necessary to subscribe to some part of the capital stock. Whether a member desiring to borrow subscribes for a number of shares which at the face value would equal the amount of his loan is immaterial. The record shows this was not required, and that fact is before this Court and needs no further finding in regard thereto. If such deprive the association of its status as a domestic building and loan association the facts are there upon which to predicate such a conclusion.

As stated in the Government's motion, the Revenue Act of 1918 exempted from taxation "domestic building and loan associations," without conditions. That act was in force until November 23, 1921, and its language was identical with the Revenue Act of 1916 and the Revenue Act of 1913 in respect of the exemption of these associations. During all of that period no requirement had ever been laid down limiting exemp-

tion only to associations which require borrowing members to subscribe to stock in an amount equal to the amount of the loan desired. With that being the situation from 1913 until 1921, we find that when the bill proposing the Revenue Act of 1921 was presented in the Senate from the House of Representatives, it proposed to exempt the same domestic building and loan associations, but added one restriction by which thereafter exemption was limited to "domestic building and loan associations *substantially all of whose business is confined to making loans to its members.*" Since 1921 that has been the law. When this bill, however, was presented in this form to the Senate, a committee amendment was offered providing for the addition after the word "members" the following words: "on the basis of their stockholdings," so that the exemption paragraph relating to building and loan associations would read:

> "Domestic building and loan associations substantially all of whose business is confined to making loans to its members *on the basis of their stockholdings.*"

This proposed amendment adding the language in italics was rejected (Congressional Record, Vol. 61, pages 7649-7653) for the reason that it was not intended to legislate to produce such a result. Senator Willis of Ohio, speaking of the amendment, stated:

> "There are two very serious objections to that (the committee amendment). The first is that it will again throw the whole matter into litigation, because I do not think anybody can

> tell what the phrase 'loans to members on the basis of their stockholdings' means. Does it mean, if one man owns a $1 share and another owns a $5 share, that loans must be proportionate, or what does it mean? Inasmuch as the question has been threshed out, and inasmuch as the financial situation in Ohio, as elsewhere, is exceedingly delicate, as Senators must know, I suggest that it would be exceedingly unwise at this time to undertake to change a situation which is fraught with the very gravest dangers."

It will, therefore, be seen that what the Government is now contending for, even relating to acts prior to 1921, was actually presented to the United States Senate and definitely rejected. There can be no question, therefore, of the intention of Congress not to place any such requirement upon an association in order that it may be entitled to exemption. But if that be not sufficient your attention is invited to the case of Acklin *vs.* Peoples Savings Association, 293 Fed. 392, wherein the U. S. District Court for the Northern District of Ohio was called upon to interpret this identical paragraph of the Revenue Act of 1921 and the exact contention now being made in this motion by the Government. That court delivered its opinion August 23, 1923, and, with the clearest exposition of the intention of Congress, decided against the Government, holding that there was no vestige of authority under the 1921 Act, which is identical with all subsequent acts, for limiting the exemption of these associations to only such which require a member to

subscribe in stock at its par value to the full amount of a loan which he may happen to desire. It held that under the statute it was only required after the passage of the 1921 Act to confine its loans to members and that as Congress did not see fit to define or limit the classification of membership a member of such an association was one which complied with its constitution and by-laws within the charter and the law authorizing the association to do business.

5. Finally, the Government claims that it needs one more additional finding of fact and that is that the number of depositors in every one of the years under consideration exceeded the number of stockholders of the association, the difference being small in 1918, but twice as great in the other years. Let us apply the test to this.

The Court of Claims has found in its Finding VII (R. 9, Item 6 of Liabilities) the amount of deposits each year. What possible assistance it could be to the Government or to this Court to know whether these deposits were made by fifty or by seventy-five different individuals is beyond conception and no reason for it is given. In its Finding VIII (R. 10) the Court of Claims has set forth the number of members each year to whom loans were made. Of what aid is it to this Court to know how many other members there may have been during any particular year who did not borrow any money? What has either of these things to do with the fundamental principle involved in this case? Of what assistance would it be to this Court or to the

Government if the record showed, for example, that during one particular year the number of depositors was one hundred and the number of stockholders was seventy-five? What would one do with that information if he had it? It is axiomatic that a building and loan association could not possibly exist if it accepted deposits in an *amount* exceeding that which it loaned because instead of it being able to thrive and pay its members a dividend, it would operate at a loss. Whether, therefore, the *amount* of deposits were made by fifty people or by ninety people is wholly irrelevant and whether it loaned the money deposited to 100 different stockholders or 200 is likewise wholly irrelevant.

It should be borne in mind that the number of members or stockholders of a building and loan association not only differs from year to year and from month to month, but from day to day. Practically every day some member's shares mature and his loan becomes paid up and he no longer remains in the association as a member. The shares that he had may then be issued to someone else who desires to become a member. At the bottom of page fifteen of the Government's motion it is apparent that what it desires to have found and placed before this Court is the number of stockholders that happened to be such on December 31st, of each year, and the number of depositors that happened to be on the books of the association on the last day of the year. There is no evidence in the record in the court below, none was presented and none could ever be produced at this late date to show how many stockholders there actually were during each day of

each one of these particular years. The depositors remain fairly constant throughout the year except that one may withdraw his deposit at any time; but the number of stockholders on the last day of the year would only represent the number on that day. There were, therefore, 364 other days in each one of these years and the number of stockholders on each one of those 364 days in each one of the years concerned was different from what it was on the last day. Doubtless if all of the stockholders on each day throughout the year were totaled, they would be far in excess of the number of depositors; but what difference would that make and of what assistance would that be to this Court? We submit that it would serve no other purpose than to clog the record.

Even if the alleged additional facts sought by this motion had not actually been found by the Court of Claims we would unhesitatingly consent that this Court may deem to have been found every single *fact* sought by this motion if it would not necessitate the remanding of this case to the Court of Claims, thus resulting in the necessity for another petition for a writ of certiorari being filed and the postponement of decision by this Court for perhaps another year. In so far as the respondent is concerned this Court is at liberty, if it deem it to be material and necessary for its determination, to consider as having been found by the court below every single *fact* covered in the motion if it has not already been competently found by the Court

of Claims; but it is respectfully submitted that there is no merit to the motion for the reasons stated and the same should be denied.

L. L. HAMBY,
Attorney for Respondent.

(3541)

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ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

BRIEF FOR RESPONDENT.

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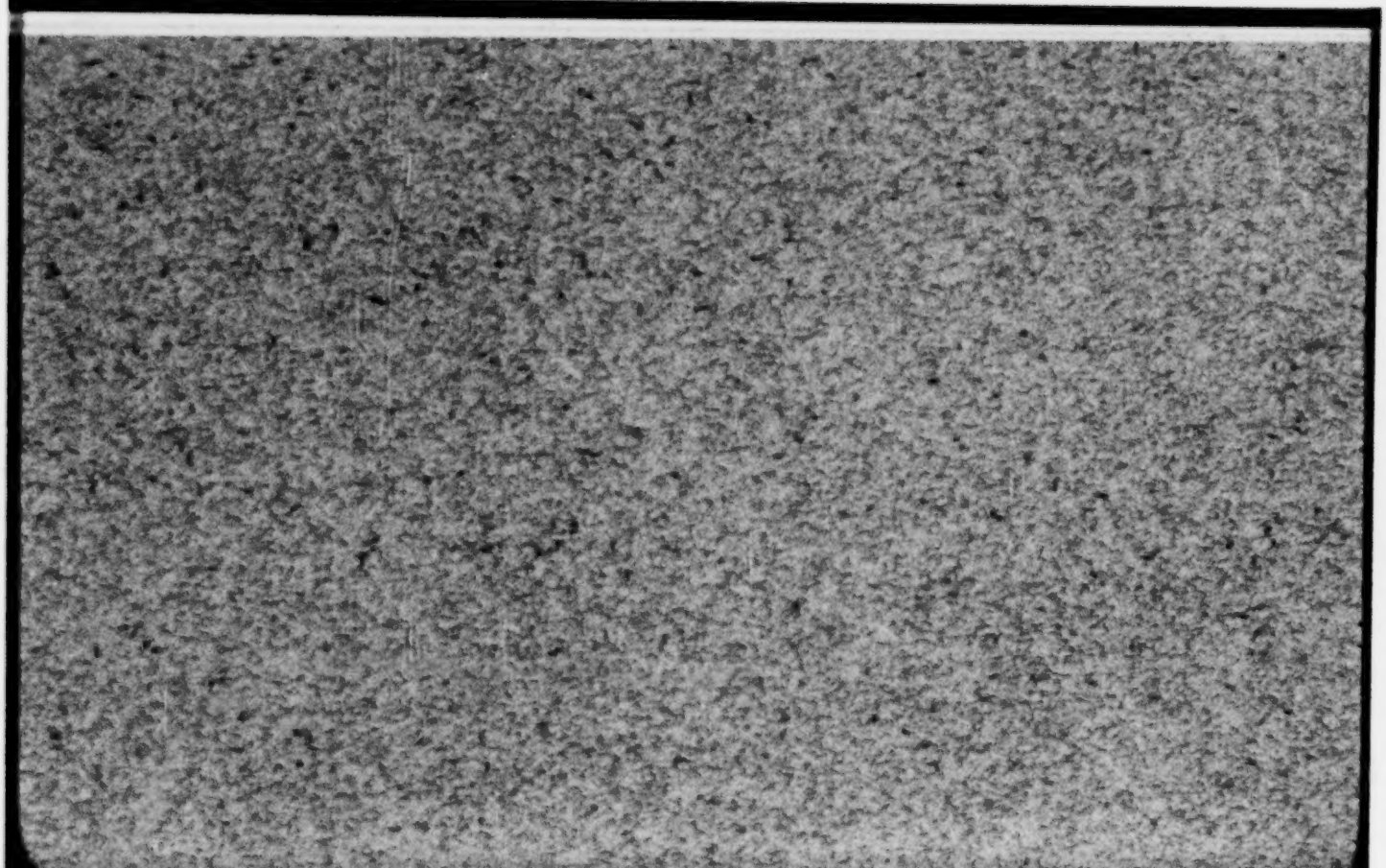

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ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

BRIEF FOR RESPONDENT.

This case presents for determination three distinct major questions of law, namely:

1. Is the respondent exempt from income and profits taxes under the Revenue Act of 1918 for the calendar years 1918 to 1921, inclusive, as a "domestic building and loan association"?

2. Is the respondent exempt from income taxes under the Revenue Act of 1921 for the calendar years 1922 and 1923 as a "domestic building and loan association substantially all of whose business was confined to making loans to its members"?

3. Is the status of the respondent for the calendar year 1921 in respect of exemption controlled by the Revenue Act of 1918 or the Revenue Act of 1921?

The Court of Claims has held that respondent is exempt under the 1918 Act as a domestic building and loan association; that it is exempt under the 1921 Act as such an association which confined its business substantially to making loans to its members, and that for the calendar year 1921, up to November, 1923, of that year, its status is controlled by the Revenue Act of 1918 and for the remainder of the year by the Revenue Act of 1921.

Since we are dealing with statutes we shall approach the questions in the light of the rules laid down by this Court for their interpretation.

While there were similar statutes dealing with the exemption of building and loan associations enacted in 1866, 1894, and 1898, the present series of tax measures which has been uninterruptedly in effect for the past nineteen years had their origin with the enactment of the Act of August 5, 1909 (36 Stat. 112). This was followed by the Act of October 3, 1913 (38 Stat. 192), which remained in effect until September 8, 1916, when the Revenue Act of 1916 was enacted (39 Stat. 756). The 1916 Act remained in effect until Feb-

ruary 24, 1919, when the Revenue Act of 1918 was enacted (40 Stat. 1057). The 1918 Act, one of the statutes herein involved, remained in effect until November 23, 1921, when the Revenue Act of 1921, also involved herein, was enacted (42 Stat. 227).

The following are the provision for exemption of these associations contained respectively in these several acts:

The 1909 Act.

This Act provided at Section 38 that nothing therein contained shall apply to

> "Domestic building and loan associations *organized and operated exclusively for the mutual benefit of their members.*" (Italic letters supplied.)

The 1913 Act

This Act provided, at Paragraph (G) of Section II, that nothing therein should apply to

> "* * * Domestic building and loan associations. * * *"

The 1916 Act.

This Act at Section 231 thereof provided:

> "That there shall not be taxed under this Title any income received by—
>
> "4th. Domestic building and loan associations *and co-operative banks without capital stock organized and operated for mutual purposes and without profit.*" (Italic letters supplied.)

The 1918 Act.

"SEC. 231. That the following organizations shall be exampe from taxation under this Title (Part. III, Corporations):

"(4) Domestic building and loan associations *and co-operative banks without capital stock organized and operated for mutual purposes and without profit.*" (Italic letters supplied.)

The 1921 Act.

"SEC. 21. The following organizations shall be exempt from taxation under this title—

"(4) Domestic building and loan associations substantially all the business of which is confined to making loans to members; and co-operative banks without capital stock organized and operated for mutual purposes and without profit."

And in Title I, Section 1, certain definitions, of which the following are pertinent:

"That when used in this Act, the term 'domestic' when applied to a corporation or partnership means created or organized in the United States"; and

"The term 'United States', when used in a geographic sense, includes only the States, the Territories of Alaska and Hawaii, and the District of Columbia"; and

"The term 'corporation' included associations, joint stock companies, and insurance companies."

This Court has remarked: "One page of history is worth a volume of logic."

It is therefore appropriate to review the history of the particular legislation relating to exemption of these associations, the judicial interpretation and executive construction of the immediately preceding Acts in *pari materia*, in order to ascertain the intention of the Congress when on February 24, 1919, it enacted the Revenue Act of 1918 which controls this case for the several years 1918 to 1921, after which it will be simple to ascertain the intention of Congress when on November 23, 1921, it enacted the Revenue Act of 1921, which controls this case for the years 1922 and 1923.

I

The 1918 Act.

History of the Legislation

Beginning with the 1909 Act, we find that it exempted from taxation domestic building and loan associations *organized and operated exclusively for the mutual benefit of their members*.

Under this Act the Commissioner of Internal Revenue undertook to, and did, assess and collect taxes from these associations, resulting in the institution of several suits by the associations to recover the taxes paid (Parkview Building & Loan Association *v.* Herold, 203 Fed. 876, affirmed in Herold *v.* Parkview Building & Loan Association, 210 Fed. 577; Bellefontaine Building & Loan Co. *v.* McMaken, and Central Building, Loan & Savings Co. *v.* Bowland, 216 Fed. 526).

In the first of these cases, Parkview Building & Loan Association *v.* Herold, *supra*, the principal question was whether under the plan of operation of the association any inequality in the returns of the prepaying shareholder and the other shareholder in favor of the one or the other destroyed the mutuality among the shareholders required under the 1969 Act. The court held that it did not, using the following language:

> "Mutual credits are not necessarily equal credits; mutual debts need not be equal in amount. That the issuance of prepaid shares does not destroy the mutuality among the members of a building and loan association is the opinion of Judge Endlich, whose work on Building and Loan Associations is deemed an authority, as may be seen in his discussion of the subject in paragraphs 461 to 464. That view is also taken by the Supreme Court of Pennsylvania in Folk *v.* State Capitol Savings & Loan Association, 214 Pa. 529, 63 Atl. 1013, where the Supreme Court affirms the lower court, which was presided over by Judge Endlich. The following quotation from Judge Endlich's opinion in that case is helpful. He says (214 Pa. 535, 63 Atl. 1016):
>
> "'That the allowance of a fixed dividend upon such paid up stock out of the profits of the corporate business is a reasonable incident to its issuance, just to both classes of shareholders, and not calculated to give either an undue advantage over the other; that, on the contrary, the practical effect of the concurrent issuance of both installment and full paid stock is likely

> to prove beneficial to both classes of shareholders; that no essential characteristic of the building association scheme can be regarded as forbidding, and no essential purpose of it as defeated by this device; that it is contrary to no accepted rule of policy applicable to or involved in the nature of building associations.' "

This case was decided March 12, 1913, before the passage of the Revenue Act of 1913 and the decision was affirmed by the Circuit Court of Appeals for the Third Circuit on January 23, 1914, in Herold *v.* Parkview Building & Loan Association, *supra*.

The last case arose in the State of Ohio, being Central Building Loan & Savings Co. *v.* Bowland, and Bellefontaine Building & Loan Co. *v.* McMaken, *supra*, wherein again the exemption provision of the 1909 Act was at issue. There *the principal questions now before this Court* were disposed of. These questions as stated by the court are:

> "The allegations in the respective petitions which raise the question to be decided are, as to the first named plaintiff, 'that plaintiff for the mutual benefit of all its members *receives deposits from, and loans money to persons who are not members*, said acts being duly authorized by the law of Ohio;' and, as to the second named plaintiff, 'that since its organization said plaintiff has by its constitution provided that it is organized for the purpose of *raising money to be loaned to its members and to others and for the purpose of receiving money on deposit from time to time to the extent necessary to meet the demand made on it by its members, depositors*

and others; that, since its organization, said plaintiff has by its by-laws provided for the carrying out of each of said purposes, and has, from time to time, received deposits upon which it paid to the depositors the amount of interest due thereon, in accordance with the rate and terms upon which the deposits were made; that notwithstanding the said provisions of its constitution and by-laws authorizing the same, it has not made any loans to others than its members; and by virtue of the laws of the state of Ohio the plaintiff is, and at all times has been, authorizd and empowered to make loans to persons who are not members and to receive deposits from persons who are not members and to pay interest on deposits made by such persons.' The plaintiffs claim exemption from the tax under the proviso in the act. The government denies exemption on the ground, as to the first named plaintiff, that '*the corporation makes loans to and receives deposits from other than members*, and that accordingly in addition to its mutual features it does a business akin to a general banking business;' and, as to the second named plaintiff, that it is a corporation 'organized for the purpose of raising money *to be loaned to members and others*, and *that it is qualified to receive deposits or borrow funds from others than members*,' 'and, therefore, the government claims that these associations cannot be considered as organized and operated for the 'exclusive benefit,' or 'exclusively for the mutual benefit,' of their respective members. The government admits that the plaintiffs are domestic building and loan associations having features of mutuality between their members."

That is exactly the case at bar, and it is important to note the conclusions reached on the two principal questions involved:

> "If the power to borrow and loan from and to others than members takes building associations having it out of the class entitled to exemption, then the building and loan associations of most of the states must pay the tax. Since Congress by using the adjective 'domestic' necessarily had in mind associations formed *under State laws*, and since almost all such institutions have such powers under those laws, it may be said with some degree of certainly that Congress did not intend to deny them the exemption they otherwise would have simply because they had power to loan to persons not members, or to borrow from them."

Speaking of the Government's contention that an association accepting deposits and making loans to nonmembers is thereby engaging in the banking business, the court said:

> "Under this definition every building association is a bank, since it receives deposits, and, indeed, lends money to its members and, in most of the states, to persons not members. But they are building associations nevertheless, whose profits inure exclusively to the members themselves, and whose power and practice of borrowing money from nonmembers and lending to the same are only incidental to the main purpose for which they are formed, and are beneficial to, and in furtherance of, that purpose.

> "A nonmember borrowing or lending receives no benefit from the building association as such, but only the same benefit which he would receive by dealing generally with his money in the market. So he in no sense participates in the association, or in its profits. This participation is the exclusive right of each of the members, and every member receives the same benefit accruing to every other member. By this method of acquiring additional income for the association, there is no disturbance of the mutuality of interest, which is the distinguishing feature of building associations; indeed, by indulging in it the essential principle to that end underlying building associations is maintained."

On the subject of the effect of issuing different classes of stock the same court had this to say:

> "And it was held that such practice did not defeat equality and mutuality among the members of the association. If, under such circumstances as these and the other cases heretofore cited on the effect of the issuing of different classes of stock upon mutuality among members of the association, that quality is not impaired, how can it be successfully claimed that the necessary mutuality is destroyed when money is borrowed or loaned from or to persons who in no event are interested in the profits or losses of the association, but to which sustain the relation only of creditor or debtor, as the case may be?"

After reviewing the laws of Ohio and pointing out in great detail the care taken by the legislature of that State to preserve the integrity of these associations

and to supervise and annually inspect their operations, the court concluded as follows:

> "The conclusion is that building associations under the laws of Ohio, notwithstanding their power to borrow money from or loan money to nonmembers, are 'organized and operated exclusively for the mutual benefit of their members,' come strictly within the proviso giving them exemption from the tax in question, cannot be required to pay it, and the plaintiffs are entitled to recover the amounts paid by them under protest."

So it is that the Ohio Federal court, interpreting the 1909 Act containing the *restrictive clause* not contained in the 1913 Act and subsequent acts, held that the acceptance of deposits from and loans to others than members unequivocally granted to building associations under the Ohio laws did not operate to deny them exemption as domestic building and loan associations *operated exclusively for the* mutual benefit of their members. No appeal was taken from the decision of the Federal court in this case and it was accepted by the Federal Government as the correct interpretation of the 1909 Act. *The 1913 Act.* When the 1913 Act was introduced in the House of Representatives the exact language of the 1909 Act was incorporated restricting exemption of these associations as before to those *organized and operated exclusively for the mutual benefit of their members.* (H. R. 3321, April 21, 1913; Sec. II(G)). On May 8, 1913, the day the bill was passed by the House, the restricting clause in-

dicated in italics was deliberately stricken out and thus passed by the Senate, so that the Act simply provided that nothing therein should apply to "domestic building and loan associations."

Thus the 1913 Act exempted these associations without condition, provided only that they be "domestic." This act was in effect until September 8, 1916, and at no time thereunder was any building and loan association in the United States required to pay income taxes. The Government never disputed their unconditional exemption, and there is no case on record bringing in question their unconditional right to exemption under this act. This was the situation when on September 8, 1916, Congress enacted the Revenue Act of 1916.

The 1916 Act. This legislation began with the introduction of H. R. 16763, 64th Congress, 1st session. In Section XI (*a*) this bill provided for the exemption of "domestic building and loan associations," which was a reenactment of the 1913 Act, under the circumstances and conditions which existed, as have been pointed out. Bear in mind that the House bill also provided for the exemption of a number of other kinds of corporations that had not been previously exempted. This is called to your attention merely to show the increasing liberality of legislation in this regard. In this manner the bill passed the House, the same language being used as had been used in the 1913 Act. When the bill reached the Senate, we find that the Senate proposed an amendment to the House bill, known as amendment number 65, whereby the Senate sought to exempt *another kind of corporation* which had not been exempted by the

House bill, and this additional corporation it proposed to exempt in the same section with building and loan associations. To this amendment the House disagreed and the Conference Committee was then called upon to consider it, and we quote from page 4 of the Conference Report, dated September 7, 1916, being report number 1200, the following language:

> "Amendment Numbered 65.—'That the House recede from its disagreement to the amendment of the Senate numbered 65, and agree to the same with an amendment as follows:
>
> "'In lieu of the matter inserted by said amendment, insert the following: "and cooperative banks without capital stock organized and operated for mutual purposes and without profit, and a semicolon;" and the Senate agreed to the same.'"

Since the House bill contained only the language in the exemption clause "domestic building and loan associations," it is plain that the additional language agreed by the Conference Committee as offered by the Senate has nothing to do with building and loan associations, for the language which was added to the House bill was "and cooperative banks without capital stock, etc."

But if any doubt be entertained as to the purpose and intention of Congress, we refer to page 29 of the Conference Report, which contains the statement of the managers, on the part of the House, concerning their agreement in conference with the Senate. There

we find the explanation of the managers of the House of their agreement with the Senate on Amendment No. 65. This is the language used:

> "The Senate amendment provides that the income of cooperative banks organized and operated for mutual purposes and without profit shall be exempted from the income tax provision. The House recedes from its disagreement to the Senate amendment with an amendment exempting cooperative banks without capital stock organized and operated for mutual purposes and without profit."

The 1916 Act was in effect until February 24, 1919, and at no time that it remained the law was any effort made to subject any building and loan association to income taxes nor is there a case on record where there was brought in question their unconditional right to exemption. Under this Act the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, issued on Jan. 2, 1918, Regulations 33 (Revised) wherein at Article 68, paragraph 313, it was provided:

> "Par. 313. Unconditional.—Among the corporations exempt from the tax, without condition are * * * domestic building and loan associations, * * *"

And at paragraph 314 it was provided:

> "In all cases wherein the exemption is without condition and the Collector is satisfied that the organization comes within the exemptive

class he will be authorized to eliminate it from his list and relieve it from the necessity of making returns.

And at paragraph 315 it was provided:

"Corporations exempt under the Act of September 8, 1916, are also exempt from the war income tax imposed by Title I of the Act of October 3, 1917."

And at Article 70 of the same Regulations it is provided:

Art. 70. Domestic Building and Loan Associations.—A domestic building and loan association entitled to exemption is one organized under and pursuant to the laws of the United States or under and pursuant to the laws of some State or Territory thereof, and which is actually carrying on for the benefit of its members a building and loan association business in accordance with the laws under which it is organized. The fact that such an association issues fully paid or prepaid shares, calling for a specified rate of interest or dividends, will not disqualify it for exemption. The exemption is without qualification other than that the association is a domestic building and loan association. If a corporation by any other name is carrying on an exclusive building-and-loan business, before it is entitled to exemption it will be encumbent upon it to show to the satisfaction

> of the commissioner of internal revenue that it is in fact a building and loan association.

It is obvious that building and loan associations no longer occupied the attention of the executive department as they were unconditionally exempted and their names taken off of the Collector's list of taxable corporations. It is interesting to note that while this 1916 Act was still in effect the Commissioner of Internal Revenue was requested to furnish a ruling to the Building and Loan Commissioner of the State of California in respect of the exemption of certain kinds of California associations which, under the law, were empowered to and did make loans to others than shareholders and members and in respect of other associations that issued permanent or guarantee stock. The ruling of the Commissioner of Internal Revenue in conformity with the request of the California Commissioner was dated January 30, 1918, and is printed in the Appendix hereto. We quote the sum and substance of the ruling:

> "In reply you are informed that Building and Loan Associations organized and operated in accordance with the laws of the State in which they are organized and do business are exempt from the provisions of the law referred to above. Therefore, if a Building and Loan Association in your State, which transacts business in accordance with the information contained in your letter, does so under the authority conferred upon it by the laws of the State of California, then that fact does not destroy its exemption under the provisions of the acts cited."

Something else occurred while the 1916 Act was in effect. The Congress, on February 26, 1917, enacted a special Act (Chap. 129 printed in full in the Appendix hereto) which directed the Secretary of the Treasury to pay to the several building and loan associations therein named (including this respondent) the sums set forth therein, the same to be a refund of taxes "illegally collected from said associations under the Excise Tax Act of August 5, 1909." This Act was to enable all associations from whom taxes had been exacted under the early 1909 Act where the statute of limitations had tolled against refund claims, to recover all such taxes. All other associations from whom such taxes had been collected had already received refunds as the result of the decisions of the Federal courts hereinbefore cited interpreting the 1909 Act.

The foregoing is the history of the legislation and of the judicial interpretation and executive construction thereof at the time the Congress undertook on February 24, 1919, to enact the Revenue Act of 1918 with which we are primarily concerned in the case at bar.

The 1918 Act was a re-enactment, without change of a word, of the 1916 and 1913 Acts in respect of the exemption of building and loan associations. What interpretation must be given the intention of Congress then when it re-enacted the prior statutes which had been judicially interpreted, and construed by the executive department, in only one way uninterruptedly for ten years?

The 1918 Act. Can it be possible in the light of the history of this legislation for anyone to doubt what Congress intended? Every rule relating to the interpretation of statutes sustains the contention of the respondent that when the 1918 Act was enacted the Congress intended it to mean the same thing that it meant when it enacted the 1913 and 1916 Acts.

The 1918 Act was in effect with all the force of the prior statutes and their interpretation behind it until November 23, 1921, when the 1921 Act was enacted. It is appropriate at this point to very briefly review some of the cardinal principles of statutory interpretation which have been laid down by this Court for the guidance of the executive departments as well as the citizens.

The Language of the Statute. In U. S. *v.* Goldenberg, 168 U. S., 95, 102, we are told:

> "The primary and general rule of statutory construction is that the intent of the lawmaker is to be found in the language that he has used. He is presumed to know the meaning of words and the rules of grammar. The courts have no function of legislation, and simply seek to ascertain the will of the legislator. It is true there are cases in which the letter of the statute is not deemed controlling, but the cases are few and exceptional and only arise when there are cogent reasons for believing that the letter does not fully and accurately disclose the intent. *No mere omission, no mere failure to provide for contingencies, which it may seem wise to have specifically provided for, justify any judicial addition to the language of the statute.*" (Italic letters supplied.)

In U. S. *v.* Temple, 105 U. S., 97, 99, this court said:

> "Our duty is to read the statute according to the nature and obvious merit of the language without resorting to subtle and forced construction for the purpose of either limiting or extending its operation."

Again in Thompson *v.* U. S., 246 U. S., 547, 551, we find:

> "The intention of Congress is to be sought for primarily in the language used and where this expresses an intention reasonably intelligible and plain, it must be accepted without modification, by resort to construction and conjecture." (See also Gould *v.* Gould, 245 U. S., 151, 153.)

History of Legislation. In Guarantee Trs. Trust & S. D. Co. *v.* Sellers, 123 U. S. 276, this Court stated that the interpretation of the statute is often to be sought from the surrounding circumstances and the preceding history.

In U. S. *v.* Union P. R. Co., 91 U. S. 72, which has been exhaustibly cited, the rule is laid down that in construing a statute the courts may recur to the history of the times when it was passed, in order to ascertain the reason for its passage, as well as the meaning of its provisions.

In Smith *v.* Townsend, 48 U. S. 490, we are told that where the language of a statute is in any manner ambiguous or the meaning doubtful, resort may be had to the surrounding circumstances, the history of the

times and the defect or mischief which the statute was intended to remedy.

In Platt *v.* Union P. R. Co., 99 U. S. 48, it was held that in construing a statute, aid may be derived from attention to the state of things as it appeared to the legislature when the statute was enacted.

In Texas & P. R. Co. *v.* Interstate Commerce Commission, 162 U. S. 197, it was held that in construing the terms of a statute courts must take notice of the history of legislation, and of different possible constructions, select and apply the one that best comports with the genius of our institutions, and therefore most likely to have been the construction intended by the law-making power.

Adding Language Not Contained in the Statute. In Hobbs *v.* McLean, 117 U. S. 567, it was held that where a provision is left out of a statute either by design or mistake of legislation the courts have no power to supply, for to do so would be to legislate and not to construe.

In Yturbide *v.* U. S., 22 How. 290, it was held that where the legislature makes plain provision without any exception, the courts can make none (see also Maxwell *v.* Moore, 22 How. 185, and Pirie *v.* Chicago Title & T. Co., 182 U. S. 438).

Contemporaneous Executive Construction. This court has held that contemporaneous construction of a statute by the executive departments should be given great consideration—certainly where it is a practical construction (see Bank of the United States *v.* Halstead, 10 Wheat. 51; Slidell *v.* Grand Jean, 111 U. S.

412; Schell *v.* Forsche, 138 U. S. 562; Prigg *v.* Pa. 16 Pet. 539; Wetmore *v.* U. S. 10 Pet. 647).

Previous Statutes in Pari Materia. In U. S. *v.* Saunders, 22 Wall. 492, it was held that it is proper in construing a statute to ascertain the intention of the legislature from the language used in connection with the previous legislation on the same subject.

In U. S. *v.* Farden, 99 U. S. 10, it was held that other acts on the same subject and the connection of the words in the Act in question may be reviewed to determine the true intent and meaning of a provision in an Act of Congress; and in Virtebo *v.* Friedlader, 120 U. S., 707, it has also been held that all former statutes on the same subject whether repealed or unrepealed may be considered in construing provisions that remain in force.

In Vane *v.* Newcombe, 130 U. S. 220, it was held that in cases of doubt or uncertainty, acts in *pari materia* may be referred to in order to discern the intent of the legislation in the use of particular terms.

Judicial Interpretation of Prior Acts in Pari Materia. This Court has held that the meaning of a particular statute should be determined in the light of prior statutes in *pari materia* that have been judicially interpreted and construed (U. S. *v.* Saunders, 22 Wall. 492; U. S. *v.* Farden, 99 U. S. 10; Crane *v.* Newcombe, 132 U. S. 220; U. S. *v.* Central P. R. Co., 118 U. S. 235; The Aurora *v.* U. S. 7 Cranch, 382).

In the light of the foregoing, it seems obvious what, as a rule of decision, must be deemed to have been the intention of Congress when it enacted the Revenue Act of 1918.

In these circumstances it is rather immaterial what the Commissioner of Internal Revenue thereafter may have attempted to do by regulation, for no such regulation could possibly change the intention of Congress at the time it enacted the 1918 Act, as we have clearly demonstrated. It is interesting, however, to note the provisions of Article 515 of his Regulations 45, quoted in full in the Appendix (page 25) to the Government's brief. These Regulations 45 so quoted were promulgated by the Commissioner and approved by the Secretary of the Treasury January 28, 1921, after the 1918 Act had been in force for about two years. There it is stated:

> "* * * Where a building and loan association has no other features which render it liable to income tax, it will ordinarily not be subject to tax merely because—
>
> "(1) It has paid-up shares which are (a) preferred as to earnings, and (b) have a definite rate of interest which may be higher than the rate of dividends paid on other stock, or
>
> "(2) Its balance sheets show that *it is lending considerable sums to nonmembers*, or
>
> "(3) It is a regular borrower of large sums of money which it uses for loans to members, the dues paid by members being entirely inadequate for the business transacted by it."

There we find as late as January, 1921, the Commissioner acquiesces in the practice, which the Government now deprecates, of lending considerable sums to nonmembers, and nowhere can it be found that he

objects to the acceptance of deposits. These regulations were enacted only ten months prior to the passage of the 1921 Act. Can it be said that there existed any executive construction of this statute which placed building and loan associations in this country on notice up to January, 1921, that the making of loans to non-members or acceptance of deposits from them would debar them from exemption? The Commissioner did not so rule, nor had any court in the United States so ruled in interpreting the exemption provision of the 1918 or any preceding statute in *pari materia*.

Most particular attention is now invited to the next regulations promulgated by the Commissioner of Internal Revenue under this same 1918 Act quoted in full in the Appendix to the Government's brief (pages 26 and 27). These subsequent regulations were promulgated and approved June 16, 1921, six months after the regulations which we have just discussed. There we find in sub-paragraph (2) that he objects to accepting deposits unless they be used only for the purpose of making loans to members, and in sub-paragraph (3), while he still sanctions the making of loans in considerable sums to nonmembers, he states that it may only be done "in times of small demand" (whatever that means), and he has no objection "in times of small demand" to the investment of the association's funds (in what manner he does not state), which would otherwise lie idle and unproductive. In the second paragraph of sub-paragraph (4) he further, for the first time, informs these associations that where the facts show that they are borrowing large sums

of money from nonmembers with no reference to the borrowing needs of members and are loaning these sums to nonmembers, the number of depositors being disproportionate to the number of members (whatever that means) and the amount loaned to nonmembers being disproportionate to the amount loaned to members, such association will be deemed to be taxable and will be granted exemption only upon a satisfactory showing to the Commissioner "that it is, in fact, a *bona fide* building and loan association within the meaning of *this article*."

What force as a criterion upon which to establish long standing executive construction of an Act of Congress is a regulation promulgated four months before the law ceased to be in effect and two and one half years after it was enacted, especially under the circumstances which have been herein related?

This brings us to the 1921 Act, but, before passing on, it may be well to refer to the eminent authority, Judge Eudlich, whose reasoning in his work on Building and Loan Associations is in true accord with the decisions of the Federal courts, *supra*, interpreting the stringent provisions of the 1869 Act. We find at Section 313 of this work, written in 1882, the following:

> "It is said in Pennsylvania, and in Ohio, and seems to be the understanding of the law in Indiana, in Kansas, and in Massachusetts, that a building association has the power of lending its money to members only, and not to strangers. *It must be admitted that there is nothing in the reason or constitution of building associations, in favor of the doctrine. On the contrary, al-*

though it undoubtedly was their design that eventually all the members should become borrowers, in practice there is always a large portion of them who content themselves with paying, and never think of drawing out. Thus, if none but members may receive loans, the funds of the society may go begging; it may be subjected to constant losses on account of their lying idle; and the very end aimed at by the association, the speedy and profitable winding-up, be delayed by a restraint as unreasonable as the license is harmless. Yet, in the absence of special statutory authority giving that license, the doctrine denying it to building associations must be held to be established by authority." (Italic letters supplied.)

Singular it is, the author refers to the fact that at the time of writing (1882) the State of Ohio and four other States did not permit non-member loans, but the author states that whether or not an association may do this *depends upon the State statute*. However, as early as 1908, the State of Ohio by legislative enactment specifically authorized these associations to accept deposits from and make loans to non-members, and it is still the law. (See Ohio statute in Appendix.) All modern authors writing on the subject are in accord with Judge Endlich.

What do the Ohio laws provide respecting loans and deposits?

"Sec. 9647. Such corporation shall have all the powers set forth in the following sections of this chapter.

"SEC. 9648. To receive money on deposits, and all persons, firm, corporations and courts, their agents, officers and appointees may make such deposits and stock deposits, but such corporation shall not pay interest thereon exceeding the legal rate. When such deposits or stock deposits are made to the joint account of two or more persons, whether adults or minors, with a joint order to the corporation that such deposits or any part thereof are to be payable on the order of any one or more of such joint depositors, and to continue to be so payable notwithstanding the death or incapacity of one or more of the persons making them, such account shall be payable to any one or more of such survivors or survivor or order notwithstanding such death or incapacity. No recovery shall be had against such corporation for amounts so paid and charged to such account.

"SEC. 9657. To make loans to members and others on such terms, conditions and securities as may be provided by the association."

And, so it is that the Commissioner of Internal Revenue in retrospectively assessing in the year 1924 taxes against respondent for the years prior to the passage of the 1921 Act, namely, for the years 1918 to 1921, pretends that the Congress did not intend to exempt these associations under the provisions of the 1909 Act or the 1913 Act, or the 1916 Act, or the 1918 Act; that the successive re-enactment of this exemption provision over a period of 12 years was not intended as an adoption of the previous executive construction and judicial interpretation of prior acts; that he is not in any

manner bound thereby, nor by his own regulations and rulings; and that what the Congress intended and meant all along was to exempt only such associations that confine their loans substantially to members, a provision contained in the subsequent Act of November 23, 1921. The 1921 Act contained no retrospective provision respecting this exemption. This Court in the case of Shwab *vs.* Doyle, 258 U. S., 529, dealing with the subject of retrospective interpretation of statutes said:

> "If Congress, however, had the purpose assigned by the Commissioner, it should have declared it; when it had that purpose, it did declare it."

And further:

> "It is to be remembered that we are dealing with a tax measure, and whatever doubts exist must be resolved against it."

And further:

> "It is the proclamation of both that a statute should not be given a retrospective operation, unless its words make that imperative and this cannot be said of the words of the Act of September 8, 1916."

And further, in respect of the question of whether the declaration in the subsequent act was intended to express the purpose of the prior act, the court said:

> "And we cannot accept the explanation that this was an elucidation of the Act of 1916, and

> not an addition to it as averred by defendant, but regards the Act of 1918 rather as a declaration of a new purpose; not the explanation of an old one." ~~Court of Claims opinion~~.

Clearly, the 1918 Act and its predecessors are dead issues and cannot be revived at this late date by an attempt of the Internal Revenue Commissioner to place an interpretation thereon directly contrary to the intention of Congress, which has repeatedly re-enacted this statute in the light of prior executive construction and judicial interpretation of prior statutes in *pari materia*.

II.

The 1921 Act.

Now, on November 23, 1921, Congress decided to continue exempting these associations as they existed, upon condition that thereafter they confine their loans substantially to their members. Thus, the 1921 Act exempts the same associations which had been exempted from tax under every prior income tax law, or such of them as, in the future, confine their business substantially to making loans to members. In all other particulars and in all other respects Congress adopted the interpretation of the previous acts. It did not see fit to place any further restrictions upon them, such as prohibiting them from accepting deposits or requiring borrowers to subscribe to stock to the full amount of their loans, or to direct how they shall operate or conduct their business, or to in any way inter-

fere with the common practice existing among the associations in the various States other than in respect of the persons to whom they may make loans. The interpretation, therefore, of the 1921 Act becomes rather simple and requires only a practical determination of the extent to which these associations, after the passage of the 1921 Act, may indulge in making loans to nonmembers if they would retain their exempt status.

The Court of Claims has held that respondent, subsequent to the passage of the 1921 Act, has substantially complied with its provisions. Has it committed gross error? Is its judgment unsound or its conclusions illogical?

There are only two years (1922 and 1923) involved herein which are controlled by the provisions of the 1921 Act.

Bearing in mind that this act was passed only five weeks before the year 1922, and that its numerous provisions are not at once broadcast among the people of the cities, towns, and hamlets of the country, let us see what the facts are as found by the court. During these two years 90% of its loans and 87% of the money loaned was to members (see years 1922-1923—Finding VIII, Rec. 10). The Government contends that too large an *amount of money* was loaned to nonmembers during these two years. The question involves material rather than arbitrary consideration, bearing in mind the circumstances and necessities of the association upon the advent of the new act. If it has not grossly or materially overstepped the bounds

of a reasonable interpretation of the statute, it should not be denied exemption.

The word "substantially," used in the 1921 Act in respect of the making of loans to members, has been defined in "Words and Phrases, 2d Series, Vol. 4, page 753," as follows:

> "'Substantially' means in substance; in the main; essential; by including the material or essential part. See Town of Checotah *vs.* Town of Eufala, 110 Pac., 1014, 1019; Vannest *vs.* Murphy, 112 N. W., 236, 238; 135 Iowa, 123. See also Electric Candy Machine Co. *vs.* Morris, 156 Fed., 972, 974; Eisfeld *vs.* Kenworth, 50 Iowa, 389, 390."

In the case of South Penn Oil Co. *vs.* Knox, 69 S. E., 1020, 1021; 68 W. Va., 362, there was involved an oil and gas lease, describing the premises as being all that certain tract of land situated in a certain district of the waters of a designated stream bounded "substantially" as follows, etc. The court held that the word "substantially" there was intended to mean "about" or "in the main," as designated, and not "wholly" or "completely."

The courts have had occasion to consider what is meant by the words "substantially all" as used in a taxing statute, namely, the Revenue Act of 1918 which provided that consolidated returns of income and invested capital should be filed by affiliated corporations; and it defined affiliation to be, *inter alia*, where one corporation owns or controls "substantially all" of the stock of another corporation. This par-

ticular provision of the 1918 Act was before the U. S. District Court for the Eastern District of Missouri in the case of *In re* Temtor Corn & Fruit Products Co., 299 Fed. 326. After due consideration of the various contentions of the Government and the taxpayer the court reached the following conclusion:

> "The Commissioner, then, had no power to say, as he has said by his regulation, that 'substantially all of the stock of the other' means '95 per cent of the voting stock'. It is a matter for the courts to construe and not a matter about which the Commissioner may promulgate a regulation binding upon the courts.
>
> "Here in this case all of the voting stock was held by the bankrupt, though there were some 3,000 other stockholders holding preferred stock, which had no vote until dividends were passed for a stated period. I readily appreciate that the control of one corporation over another is ordinarily had by reason of control of the voting stock therein, and not through control of the non-voting stock. It is also true that no one is to be taxed, unless there exists a statute which authorizes the imposition of the tax. Such a statute is, however, to be given a reasonable construction, when it in fact exists, with a view to carrying out its purpose and intent. Here the purpose of Congress was to forestall such manipulation of profits of one corporation, through control by reason of voting stock, as would prevent the government from ascertaining correctly, and from collecting the sums justly due it, from excess profit taxes, of the controlled and affiliated corporations."

In conclusion the court observes:

> "From what is said, it follows that the construction of the word 'substantially' is also a matter for the courts, however valuable as a rule of practice and administration it may be to have fixed by the Commissioner a merely arbitrary standard."

It should be noted that the Commissioner has never attempted in any regulation to say what was meant by the words "substantially all" in the exemption provisions of the 1921 Act with which we are dealing.

The case just cited was appealed to the Circuit Court of Appeals for the Eighth Circuit and is reported as Schlafly v. U. S., 4 Fed., 195, wherein the decision of the District Court was affirmed.

It would seem to us that we must give these same words used in the exemption provisions of the 1921 Act some material, reasonable construction or else we must assume that Congress intended that they should be construed arbitrarily. If they are to be construed arbitrarily it presents indeed a difficult task requiring the selection of some particular percentage or proportion, such as more than a half, seventy-five per cent, ninety five per cent or it may be ninety-nine per cent. If, however, we consider the subject-matter and endeavor to reach some conclusion as to what was reasonably intended, our duty becomes something more than that of making a selection or drawing in a lottery.

Of course, in due time all of these associations became aware of the provisions of the new law, so that within a few months after the advent of the new ex-

emption provision it became a very simple matter for all of them to comply therewith and, except for the year 1922, the question now under discussion is purely academic. All that was necessary to be done after the provisions of the new law became known was for associations to require all borrowers to become members by subscribing to stock. (See Acklin *v.* Peoples Savings Association, 293 Fed., 292.)

III.

Is the Year 1921 Controlled by the 1918 or 1921 Act?

While no argument was made on this subject in the brief of the Government it has assumed that the 1921 Act controls the year 1921. This we dispute.

As we have heretofore shown, all Acts prior to the 1921 Act exempted these associations without condition, so that they were not required to confine their loans to members in order to be exempted until the 1921 Act was passed. The 1918 Act was in full force and effect until November 23, 1921, only five weeks before the end of that year, and up to that moment associations could not be denied exemptions upon the ground that they made loans to others than members. When, on November 23, 1921, Congress enacted the 1921 Act did it intend by any provision of the exemption clause to take away that which had already been granted, or did it intend prospectively in respect of the exemption clause to limit it to associations who in the future confined their loans substantially to members?

The 1921 Act provided at Section 231(4) that building and loan associations which confine their loans substantially to members shall be exempt from taxation under that Act. No language can be found in the entire exemption section indicating an intention to take away an exemption which had already vested in these associations up to the passage of that Act. The only reason for the assumption indulged in by the Government is to be found in Title XIV relating to repeals, where, at Section 1400, it was provided that Title II (relating to income tax) of the Revenue Act of 1918 is repealed as of January 1, 1921. This, we say, Congress intended to relate only to those who by the terms and the provisions of the 1918 Act were *subject to the tax* and not to those which had been exempted up to the date of the passage of the 1921 Act. This seems clear in view of paragraph (*b*) of Section 1400, which continues the 1918 Act in force, for the assessment and collection of all taxes which have accrued under that Act (as to those *subject* to the tax) at the time such parts of the Act which are repealed cease to be in effect.

The scheme evidently intended was that in respect of those subject to the tax, the tax imposed by the 1921 Act shall be in lieu of the tax imposed under the 1918 Act except where taxes had accrued under the 1918 Act at the time the 1921 Act was passed. Many corporations may have had a fiscal year ended prior to the passage of the 1921 Act, but subsequent to January 1, 1921. Consequently the 1921 Act could not operate upon them until the beginning of their next fiscal year,

because in such cases the taxpayer's liability had already accrued and could not be retroactively changed by the provisions of the subsequent Act, or at least such was not the intention of the Act.

To give this exemption provision of the 1921 Act retrospective meaning would be to say that Congress did not intend that any building and loan association should be exempted for the year 1921, because, having properly made loans to others than members under the 1918 and prior Acts up to November 23, 1921, they would be powerless to recall those loans back to January 1, 1921, in order to comply *nunc pro tunc* with the retrospective provision of the 1921 Act. Thus we say Congress merely intended, so far as the exemption was concerned, that associations must comply with the provisions of the 1921 Act from and after its passage.

This Court has expressed itself in no uncertain terms concerning retrospective legislation, notably in the case of Shwab *v.* Doyle, *supra*, and more recently in the case of Nichols *v.* Coolidge, 274 U. S. 531. We contend, therefore, that there was no intention of Congress to retrospectively deny exemption and that the retrospective operation of the repeal provision related only to those who were subject to the tax; but if any intention to the contrary can be found then we say that the Congress was without authority to take away the exemption which had been granted up to November 23, 1921.

The Court of Claims, in its opinion (R. 12), agrees with our construction, stating:

> "The Act of 1918 is applicable to the years 1918, 1919, 1920, and from January 1 to November 23, 1921; and the Act of 1921 is applicable to the period between November 23 and December 31, 1921, when the act was passed, and to the years 1922 and 1923."

Again in its opinion (R. 17) it stated:

> "The Act of 1921 exempting only such associations as confined their loans substantially to members could not affect the legal status of associations operating prior thereto and under other acts which did not even require the filing of a tax return. In attempting, after the passage of the 1921 act, to enforce the collection of taxes under prior acts the Commissioner of Internal Revenue was evidently under the impression that the exemption under the prior acts was likewise intended only for associations whose business was substantially confined to loans to members. The 1921 act is not susceptible of this construction. It was operative only upon the business of such associations after the effective date of the act. It should be stated in this connection that since the passage of the 1921 act plaintiff company has substantially complied with its provisions."

So it is that unless this construction be correct, we must conclude, without any apparent reason, that the Congress intended retrospectively to take away the exemption of all building and loans associations for one single year, namely, the year 1921. Such an intention is repulsive to the history of the entire legislation.

Let us now briefly reply to such points raised in the Government's argument as may not have been fully covered herein.

On page 5 of its brief there is set forth the proportion of the deposits on hand on the last day of each year to the total assets of the association on the last day of each year. We fail to see what that has to do with the issue, since all associations have the right to accept deposits, and the amount which they may accept is governed entirely by the amount they are able to lend. Consequently, an association which accepts deposits in excess of the amount it is able to lend would soon go out of business. Practically all the associations accept deposits; the Ohio laws permit this association to accept deposits; the text book writers all maintain that they have authority to do so unless prohibited by statute; and the decisions of the courts uphold the practice. It has also been seen that up to the time of the enactment of the 1921 Act it was entirely proper for associations to make loans to others than members; the Ohio laws permitted this association to do so; all text book writers hold it to be within their powers unless specifically prohibited by the laws of the State which created them; the Departmental Regulations permitted it; and there is no decision of any court which holds to the contrary.

It should be noted that in order to endeavor to swell percentages the Government has denominated as a loan to a nonmember money which the association had deposited in a bank or deposited with other building and loan associations. One who deposits money in a

bank is not usually deemed to have made a loan, and certainly not the kind of loan which building and loan associations are accustomed to make.

The Court of Claims observed (R. 14) that this association made 40 mortgage loans to members and 39 to nonmembers in 1918; 158 to members and 47 to nonmembers in 1919; 143 to members and 70 to nonmembers in 1920; 177 to members and 30 to nonmembers in 1921; 175 to members and 10 to nonmembers in 1922; and 262 to members and one to nonmembers in 1923. Through the entire period 1918 to 1923 the Court of Claims points out that 955 mortgage loans were made to members and 197 to nonmembers. And for the entire period 1918 to 1923, the court points out that the total loans were $2,271,604.40, of which $1,488,294.28 was loaned to members and $783,310.12 to nonmembers. Thus, as the court shows, 82 per cent of the total number of loans made during the whole period was to members, and 18 per cent to nonmembers, and in respect of the total amount loaned during the whole period 70 per cent thereof was to members and 30 per cent to nonmembers, which includes the years 1918 to 1921, when the law permitted the making of loans to nonmembers.

It should also be borne in mind, as the Court of Claims has pointed out (R. 17), that since the passage of the 1921 Act this association has substantially complied with its provisions, and as shown by Finding VIII (R. 10) for the two years controlled by the 1921 Act, namely, the years 1922 and 1923, the association made 452 loans to members and 74 loans to nonmem-

bers, or 95 per cent to members; and of the total loaned in these two years $919,072.33 was to members and $124,075 to nonmembers, or approximately 90 per cent to members.

It will also please be observed (Finding VIII, R. 10) that for the entire period 1918 to 1923, 1,291 loans were made, of which 1,089 were mortgage loans on homes, farms and real estate, or 90 per cent, while only 302 were business and collateral loans and loans to churches and on apartments.

It should also be noted that at the end of the year 1923 this association had, after forty-five years in business, only $29,106.69 cash on hand, including all undivided profits, indicating that it has paid to its members for the past forty-five years practically every dollar of its earnings in the form of dividends to offset the interest payable by them on their loans and thus has enabled them at the lowest possible cost to own their own homes. No other institution in the world could boast of such a record, nor could such business be transacted for the benefit of the home owning citizen by any other class of institution in this country; and yet, notwithstanding this record and that this association has been doing business as a domestic building and loan association in the State of Ohio for forty five years without question, you are asked now to find that it is not a building and loan association and that it is operated solely for private gain or profit.

What Kind of Association Did Congress Intend to Exempt.

To sustain its contention that this association does not measure up to the standard of a building and loan association, the Government (page 9 of its brief) cites Sections 3, 7 and 17 of Sundheim on the Law of Building and Loan Associations; Sections 1 and 7 of Endlich on Building Associations; Sections 920 and 921 Corpus Juris; 4 R. C. L. 343; and Eversman v. Schmitt, 53 Ohio State 174. *Inter alia*, we rely upon the same authorities, except the last, to support the opposite contention. As to the last (Eversman v. Schmitt), we will prove it to be inapplicable.

Section 3 of Sundheim on Building and Loan Associations describes the original building and loan association as it first sprung up in this country and to a large extent what is there stated is applicable to associations operating today. Section 7 is quite applicable to these associations as they exist today. We fail to see what comfort, however, the Government can find in citing this section, for we find therein the following:

> "They are the savings bank of the small investor, and their adaptability for that purpose has been fully demonstrated. They offer the best plan yet devised for people of small means to secure their own homes and for systematic saving of small sums of money. They are the most economically conducted financial institutions in the world, and have, despite this, suffered the least financial loss. They have grown to such an extent in recent years that they no longer restrict their money to the home buyer,

but loan their money to the mere investor or dealer in real estate. They are the holders of large mortgages secured upon farms, factories and other business properties and rows of stores and dwellings. This is not an abuse of their powers or a departure from their main purposes, but only a natural and proper expansion along healthy and legitimate lines. All legislation in recent years has been to enlarge and broaden their powers, not to confine and restrict them. The courts have been liberal in the construction of these especially delegated powers, and, as a result, they have grown and changed as conditions required. Judge Endlich, no doubt the greatest authority on these institutions, well says: 'It is, indeed, to be noted that the legislature has attempted no definition of what constitutes a building association. It has assumed that certain features and methods are essential to it, and there is no room for doubt that without them no corporation, whatever its label, can claim to be a building association. But it has not excluded the possibility that, consistently with these essential features, the legitimate development of the business of these associations may add others which, at the date of enactment, were not foreseen and against which, therefore, it is not to be taken as implying any prohibition.'"

Section 8 of this work treats of the benefits such associations are to a community and Sections 9 to 15 give illustrations of seven different methods of operation. Section 190, dealing with the subject of taxation, gives us an idea of the reasons why these associations should be exempt from taxation.

The Government finally cites one more Section, being Section 17. There is nothing in this section that is foreign to any building and loan association in the State of Ohio, and certainly not to the case of this respondent.

Permit us now to direct your attention to a few other sections contained in this work of Mr. Sundheim dealing more directly with the matter in dispute.

At Section 9, page 25, the author deals with different plans of associations as they exist and operate under different State statutes.

At Section 111, page 112, the same author states:

> "Loans are made for the purpose of purchasing a homestead, or *other real estate, or for any lawful purpose or business, but there is no duty or obligation of the association to inquire for what purpose the loan is obtained, or to require any stipulation upon the borrower as to what use he will make of the money, or in any manner to supervise or control its disbursement.*" (Italic letters supplied.)

The Government (page 9 of its brief) next cites Sections 1 and 7 of Endlich on Building Associations. We have already quoted (*supra*) from that authority in respect of the matter of the authority of these associations to make loans to nonmembers (Sec. 313).

At Section 1, Judge Endlich, writing in 1882, furnishes us with an introduction to the subject of his treatise and at Section 7 he gives us an insight into the general scheme of operation of the original building association, none of which is questioned.

We have already quoted from Section 313 dealing with loans to nonmembers and we now refer to Section 77 dealing with the matter of accepting deposits, where the author states:

> "There is, where it is permitted by law to exist, a class, known as 'depositors,'—persons who, without entering the circle of the society's membership, and becoming liable to all its duties, and sharing in all its benefits, use its treasury as a savings bank, in which to deposit, from time to time, small sums of money, with the privilege of drawing them, at their pleasure, thereafter under certain restrictions, and with the addition of interest at a certain moderate rate. These people are not members. Their status depends entirely upon statutory provisions; for, without such, the society has no right to take their money, and the safety of their own deposits is materially imperiled."

The right of this and other associations in Ohio to accept deposits is regulated by the Ohio General Code, in effect during the entire period here involved—Section 9648. (See Appendix.)

Attention is invited to Section 311 of Endlich on Building Associations, where the author deals with the manner in which associations may invest their funds, and compare this with the rigid restrictions of the Ohio laws in regard thereto. (See Ohio laws, Secs. 9660, 9661, 9662—Appendix.)

The Government next cites 9 *Corpus Juris*, 920, 921. These sections deal with the origin and growth of these associations and their history wherein there is

portrayed only the original purpose and scope of authority of these associations.

We now invite attention to 9 *Corpus Juris*, 922, where we find the following:

> "The main features of the plan of the ordinary building associations have already been set out in the definition" (this is what the defendant has quoted), "and in some cases the courts have described with more or less detail the plan and mode of operation of such associations and societies; but while the general plan and purpose of all such associations is the same, yet *because statutory regulations are meager in some States and abundant and detailed in others, their methods of transacting business are by no means uniform*, and the decisions of the courts passing on their transactions are far from being harmonious. Also the character of mutuality required is not always the same under different statutes."

We also invite attention to page 923, Section 8, which states:

> "While building and loan associations originated at an earlier date, it was not until about the middle of the nineteenth century that the States generally enacted statutes authorizing their incorporation, granting them privileges, and regulating their business. By virtue of its police power the State may regulate building and loan associations even to the extent of limiting the carrying on of their business to incorporated associations or to the extent of making the State auditor a general supervising officer over this class of corporations."

We also call attention to page 954, Section 70, where we find that where there is express statutory authority, a building and loan association may make loans to nonmembers, and may, unless its power is restricted by statute, loan money for other than building purposes, and that it is not required to ascertain the use to which a borrowing member intends to apply the money.

Next the Government cites 4 R. C. L., 343. Section 2 thereof relates to the building society as it was first organized and the author's of that work follows in general what all of the other authors herein referred to have stated and to which there is in general no criticism whatever. We direct attention, however, to the last sentence of Section 2, which is as follows:

> "In arriving at a determination of the question whether a particular corporation is a building and loan association the name of the association is not material, if it has *the purposes and characteristics named in the statute authorizing the organization of such an association.*"

Finally, at page 9 of its brief, the Government cites Eversman v. Schmitt. This case was decided by the Ohio State Court June 11, 1895, at a time when the laws of the State of Ohio did not permit building and loan associations to make loans to any but members. So long as that remained the law of Ohio that case may be appropriately cited, but on May 11, 1908, thirteen years later, the Ohio legislature passed what was known as the "Russell Bill," which was the law of Ohio during all the years involved in this controversy

being set forth in full in the Appendix hereto. That law permitted associations to make loans to members and others and to accept deposits from members and others and this has been the law of Ohio for the past twenty years. The case cited, therefore, is not applicable as a test of what is a building and loan association in Ohio at any time subsequent to the year 1908. It seems remarkable but true that the Government cannot find a single case arising in the State of Ohio subsequent to the year 1908 which holds that an association in that State lending to or accepting deposits from others than members is not a building and loan association. The laws of Ohio since February 21, 1867, being the first statute dealing with the incorporation of these associations, have permitted them to receive deposits either from members or nonmembers.

The Government's position is that notwithstanding the Congress has exempted *domestic* building and loan associations and has defined "domestic"; and that the respondent is such an association under the Ohio laws; nevertheless it is not a building and loan association according to common usage of the term in this country. The best answer to that is the history of these institutions. However, the real question here is what did Congress intend as may be determined by the rules of statutory interpretation.

History of Building and Loan Associations in the United States.

We will now very briefly discuss the origin and history of this character of association as it has been

known in this country, assuming that Congress in exempting building and loan associations intended to exempt them as they were known to exist and operate in the various States of the United States, since, at the time of the enactment of the Revenue Act of 1918 and for at least fifty years prior thereto, there did not exist in the United States such a thing as a common law building and loan society. All of them, ever since at least fifty to seventy-five years before the passage of the act, owed their entire existence, including the scope of operations or methods of doing business, to the statutes of the various States enacted in respect of such associations. Associations so created and operating were the only institutions that Congress could have intended its act to operate upon because there were no other associations of the kind in this country, except those created by State statute. Congress, no doubt at the suggestion of the Treasury Department, in 1921 decided that it would no longer allow building and loan associations as they existed in the various States to be exempted, but placed one restriction only upon them. This permitted them to be exempted if they were a building and loan association under the State laws, provided, after that act became effective, substantially all of their loans were made to members. It must follow, then, as we will fully demonstrate, that until Congress placed this restriction upon exempting these building and loan associations as they existed in the States for years, where they have been exempted under every revenue act that has ever been passed, they must be given exemption up to the passage of the 1921 Act without restriction.

The first building and loan association was established in 1815 by the Earl of Selkirk, in Scotland, and the first one in the United States was organized in Brooklyn, New York, in 1836. Their growth and extension have been rapid, both in Great Britain, where an act of Parliament in 1836 greatly facilitated their formation and control, and in the United States, where they now exist in one form or another in nearly all the States. As originally created, more than one hundred years ago, not by any statute but simply by the organization of individuals, they were intended by small periodical payments to permit people of limited means to become the owners of homes, and thereby thrift, economy and good citizenship was promoted. (See 9 *Corpus Juris*, 921.) The underlying purpose, therefore, was to enable people of limited means who did not have the ready cash to be able to acquire *homes* and thereby to promote thrift, economy and good citizenship. But while the general plan and purpose of all such associations is the same, yet because statutory regulations are meager in some States and abundant and detailed in others, their methods of transacting business are by no means uniform. (9 *Corpus Juris*, 922, citing numerous cases.)

There were associations known as "terminating societies," which, by their rules, are to terminate at a fixed date or when a certain specified result is attained. This character of association does not now exist in the United States. Can we infer that Congress intended its act to relate to such a thing? There was another class, known as "serial associations," where its stock is divided into series, each series being issued

separately and maturing separately, the intervals between the issues being determined by the money on hand or by the rules of the association, and the profits or losses were generally reckoned on the whole stock and then divided equally among the different series, unless the rules provide otherwise. This kind of building and loan associations does not generally exist in the United States.

Did Congress have these in mind?

Another class is known as "the permanent association," being one which issues its stock, not all at once, nor in series, but at any time when application is made therefor, and therefore one may become a member in a permanent association at any time without any back payment of dues. This is the character of association which generally exists in this country, as modified, however, by statute in the various States. In England a permanent society is one which has not by its rules any fixed date or specified result at which it shall terminate.

It is said that while building and loan associations originated at an earlier date it was not until about the middle of the nineteenth century that the States generally enacted statutes authorizing their incorporation, granting them privileges and regulating their business. By virtue of its police power a State may regulate building and loan associations even to the extent of limiting the carrying on of their business to incorporated associations or to the extent of making the State auditor a general supervising officer over

this class of corporation. In the exercise of this power various statutes have been passed relating, among other things, to the incorporation of such societies, to their powers, to the withdrawal of stockholders and to the imposition, amount and collection of dues, fines, premiums and interest. Some of these statutes are by their terms applicable only to such associations as elect to do business thereunder, while many others regulate only foreign associations (9 *Corpus Juris*, 923D).

We also find that, in the *absence* of a statute expressly authorizing the creation of such associations, building and loan associations may be organized as voluntary associations or formed into certain corporations under the general law; but where there is a general provision for the incorporation of such societies they must be organized thereunder, and except in a very few jurisdictions where unincorporated societies have existed, the general practice requires incorporation. (See 9 *Corpus Juris*, 924A.)

It will readily be seen, therefore, that Congress could not have intended its act to relate to something which did not exist, namely, the original building and loan association, which was an unincorporated affair and which did business in an old-fashioned way not known now and not known in this country for the past seventy-five years. It must also appear, at all events, that since under the laws of all the States in the United States these associations are required to be incorporated and all of them to be regulated and controlled by a public official, whose duty it is to see that they operate and

conduct their business within the provisions of the laws of the State creating them, that this is the only kind of association Congress could have intended because no other kind existed in the United States. If that be true, by what authority does the Commissioner attempt himself to impute to Congress what *he* regards as a true building and loan association? Can he select from the States one whose laws in respect of building and loan associations seem to coincide with his particular idea of what a building and loan association should do and how it may operate and then say that Congress intended only to exempt *this* kind of association? Was any such power conferred upon him, or must he accept these associations as they have existed in the States, and particularly in the States of Ohio, for the past forty or fifty years and exempt them until and unless Congress shall either define the kind of building and loan association it intends to exempt or else until and unless Congress, while accepting these associations as they exist in the various States, shall prescribe some restriction upon their exemption which shall apply to all alike? Until the passage of the 1921 Act Congress accepted these associations as they existed in the various States. In 1921, as we have already pointed out, Congress undertook for the first time to place a restriction upon their exemption, and in doing so it accepted them as they existed in the States, provided that, regardless of the powers conferred upon them by the States, they confine their business to making loans to members.

The evidence in this case shows beyond a shadow of doubt that this association which has been steadily engaged in business for forty years as a building and loan association, known to everyone as such, has complied with all the laws of the State of Ohio, and since the creation of a superintendent of building and loan associations by that State, in the year 1891, it has been annually inspected and has received a certificate each year to the effect that it has complied with the Ohio laws relating to the conduct of the business of a building and loan association in that State. This answers the requisites of the Revenue Act of 1918, which governs the years 1918, 1919, and 1920 and until the passage of the Revenue Act of 1921, on November 23 of that year. We concede that when the 1921 Act was passed in order to be exempt this association must do one thing more than comply with the laws of the State of Ohio relating to the carrying on of business of a building and loan association, and that is it must confine its business *substantially* to the making of loans to its members. The evidence shows that from December, 1921, shortly after the passage of the Revenue Act of 1921, throughout the years 1922 and 1923, which are the only subsequent years in controversy, substantially all of its business was confined to making loans to its members, since 90 per cent of its loans in those two years were to members and 87 per cent of the money loaned was to members. (See years 1922-1923, Finding VIII, Rec. 10.)

The government on page 12 of its brief cites *Lilley Building & Loan Company* v. *Miller*, 285 Fed., 143,

also on page 14 *Appeal of Johnstown Building & Loan Association*, 6 B. T. A., 462, and *Broadview Savings & Loan Company v. Commissioner*, 10 B. T. A., 725.

The Lilley Case.

This case was cited by the government on page 12 of its brief as authority for its contention that the words "without capital stock organized and operated for mutual purposes and without profit," contained in the exemption provisions of the 1916 and 1918 Act, modifies "domestic building and loan associations" as well as "co-operative banks." For convenience, we repeat the exemption provision of those acts:

> "SEC. 231. That the following organizations shall be exempt from taxation under this Title—
>
> "4. Domestic building and loan associations *and co-operative banks without capital stock organized and operated for mutual purposes and without profit.*"

We have heretofore shown in the history of the legislation that after the 1916 Act had been passed by the House, exempting domestic building and loan associations, the Senate and the Conference Committee agreed to extend the exemption to another institution and as stated therein the purpose of the amendment was to exempt also "co-operative banks without capital stock organized and operated," etc. It is quite apparent, therefore, that this had nothing to do with the exemption of building and loan associations, as the Court of Claims has pointed out. Furthermore, no one ever heard of a building and loan association with-

out capital stock, but co-operative banks have no capital stock; and building associations are operated for profit, for the benefit of their members, whereas co-operative banks are not operated for profit. Furthermore, it is an elementary rule of grammar that a phrase or clause modifies only its immediate antecedent.

Attention is invited to the fact that the Lilley case was not decided until after the passage of the 1921 Act but it interprets the 1916 and 1918 Acts. We have pointed out the history of all legislation prior to the 1921 Act, together with the executive construction and judicial interpretation thereof, from which no doubt could be entertained of the intention of Congress when it passed the 1918 Act. It would, therefore, be incompetent four years later for any court, after the passage of a subsequent act, to place some other interpretation upon this intention. In fairness to Judge Peck, who decided the Lilley case, but who is no longer on the Bench, we wish to point out several fundamental errors in his decision of that case, due, perhaps, to the fact that the decision was based upon totally mistaken premises, to which his attention may never have been directed.

First, he proceeded upon the assumption that the 1909, 1913 and 1916 Acts were identical, whereas we have clearly pointed out that the 1909 Act contained a restrictive clause which was deliberately stricken out in the 1913 Act and never appeared in the subsequent acts.

Next, his opinion is based upon the decision in the case of *Eversmann v. Schmitt* (*supra*), which, as we have pointed out, was a decision rendered in 1895, at a time when Ohio associations were not permitted to make loans to others than members.

Next, Judge Peck relied upon the case of *Hadsell v. Union Ins. Co.*, 105 Miss., 268, which dealt solely with the interpretation of the Mississippi Constitution. In that case the court ordered a rehearing (page 280 of the opinion) and reversed its former decision, from which Judge Peck quoted and upon which he relied.

Next Judge Peck erroneously interpreted the words "without capital stock organized and operated for mutual purposes and without profit" in the exemption provisions of the 1918 Act as modifying "domestic building and loan associations," as we have pointed out.

Next it appears that Judge Peck was unaware that in 1917 Congress passed a special act ordering the refund of all taxes collected from these associations as having been illegally collected even under the stringent provisions of the 1909 Act.

We must assume that had Judge Peck not been mistaken in his premises and had he been aware of the errors upon which his decision was founded he would have reached the opposite conclusion, if he would have applied the established principles of statutory interpretation. It is only fair, however, to say that perhaps the most unusual facts which were before him in the Lilley case probably had a great deal to do with his ultimate conclusions, but we do not agree from a

legal viewpoint that even these facts should have affected his conclusions. A casual reading of the facts in the Lilley case indicates beyond question that it can scarcely be considered a precedent for any other case. The Court of Appeals affirmed the decision in the Lilley case without opinion, being evidently unaware of the fundamental errors which we have pointed out.

The Eccentric Facts in the Lilley Case.

While there are many facts of a general nature appearing in connection with the Lilley case that are applicable to all associations, yet there are several outstanding facts in that case which are not applicable to the case of any other association which has been presented for judicial determination. We will discuss, therefore, only these eccentric facts, because the court's decision must be due to them or else it must be said to have opposed the reasoning of every other court which has ever considered the principles involved in these cases. What are these facts?

First, it received deposits of nonmembers *evidenced by entries in books such as are ordinarily used by savings banks*. The style or character of the book of itself should not be of any great importance, but it probably received the consideration of the court.

Second, out of all of the loans made by the Lilley Building & Loan Association for the typical year considered by the court, only *two* were to stockholders or members of a total of four hundred ninety-five (495). In other words, only four-tenths of one per cent of its loans were made to members. That is the outstand-

ing feature of the Lilley case and that was the reason, if any there be, why that association was held not to be exempt. Upon this point the court in the Lilley case observed:

> "It is not thought that the making of loans to nonmembers or borrowing from nonmembers, or receiving deposits to be withdrawn on demand or on time, so long as such transactions are simply incidental to the primary purpose of operating a mutual building association, would defeat the exemption."

And further in its opinion, and with which the court concludes its observations upon the facts, we find:

> "It may not be possible to define precisely how far a building association may go in extraneous activities without losing its essential character, but it seems clear that when it ceases to be substantially mutual and adopts *as its chief business dealing for profit with the general public by the methods of an ordinary savings bank*, it is no longer a building association *entitled to be exempted* from income taxation under the statute in question."

The Court of Claims has very thoroughly reviewed the Lilley case and reached the inevitable conclusion that in principle it was fundamentally unsound in attempting to revive a dead issue, namely, the meaning of the 1918 Act, which, theretofore, had never had but one meaning, one executive construction and one interpretation by the courts, interpreting the prior statutes *in pari materia*.

The Johnstown case (*supra*), decided by the Board of Tax Appeals, involved the 1918 Act and the 1921

Act. The Board exempted that association for the year 1922 under the 1921 Act, but held it not exempt under the 1918 Act, using as its sole authority the decision in the Lilley case, without any reference to the history of the legislation, the executive construction, or the interpretation of the prior statutes, and without any reference whatever to the laws of Ohio, and notwithstanding the Johnstown association was admittedly a building and loan association under the laws of Ohio.

In the case of the Broadview association (*supra*), cited by the government, the years involved were controlled by the 1921 Act. There the Board in effect overruled its decision in the Johnstown case for the year 1922, where the facts were almost identical, and applied an unheard of principle of reasoning, which we will briefly set forth.

The facts in the Broadview case were that all of the loans made by the association were to members exclusively since the passage of the 1921 Act limiting exemption to associations which confined their loans substantially to members, but because in prior years *long before the passage of the 1921 Act* the association had made loans to others than members, which loans had not been completely repaid and upon which payments were still being made during the taxable year 1922, together with interest, the Board held that the receipt after the 1921 Act of such interest and payments on loans made many years prior thereto to nonmembers, being no part of the business done in 1922, constituted such business with nonmembers as to deprive it of exemption for the year 1922.

The proposition amounts to no more than this: Although an association after the passage of the 1921 Act confined its loans substantially or entirely to members, yet it is not entitled to exemption if there be found on its books outstanding loans which had been made within ten years prior thereto to others than members and upon which payments on such loans with interest were being made. This means, in effect, that if an association permits the repayment of those old loans with interest after the passage of the 1921 Act it prevents exemption. In other words, to be exempt after the passage of the 1921 Act, it would be necessary for an association to cancel all outstanding loans which may have been made from one to ten years prior thereto to others than members or else forfeit its exemption. Did Congress have in mind any such absurd intention? If it did then it did not intend its act to benefit any association, because all of them in the State of Ohio, and in most of the States prior to the passage of the 1921 Act, had the right to make loans to nonmembers and to accept deposits from them, so, naturally, upon the passage of the 1921 Act they had outstanding on their books unpaid loans as well as deposits. A building and loan association is a money lending institution and its business is making loans. What Congress meant was to confine that business in the future to loans to its members and it did not intend as a prerequisite to exemption thereafter that every association must immediately remit all deposits which it had prior thereto received from others than members and cancel all loans that had been made in the past to nonmembers.

It also appears that the Board was displeased because some of the loans made to *bona fide* members were used for other purposes thereafter by the individual. The Act places no such limitation upon exemption. (See Sundheim on Building and Loan Associations, 2nd Ed., p. 20, 22, 24, and p. 112, Sec. 111.)

Finally, on page 13 of its brief, the government refers to the case of Pacific Building & Loan Association *v.* Hartson, 201 Fed. 1011. This case is not only contrary to Parkview Building & Loan Association *v.* Herold (*supra*) and Central Building, Loan & Savings Co. *v.* Bowland (*supra*), subsequently decided, but in the latter case the fundamental error committed by the court in the case of Pacific Building & Loan Association is pointed out with unmistakable clarity.

In conclusion, we think that the very masterly, clear, and logical opinion of the Court of Claims is absolutely correct, sound, and a wholesome interpretation of the law involved, and its decision should be affirmed. Congress has the power to take away this exemption entirely at any time and certainly has the power from time to time to place such other and further restrictions upon exemption as it may deem advisable. Until it shall do so we think it is not within the province of the courts to undertake to regulate the exemption of these associations.

Respectfully submitted,

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Washington, D. C.

October, 1928.

APPENDIX.

Laws of Ohio Relating to Building and Loan Associations.

Interpretation of Terms.

Sec. 9643. A corporation for the purpose of raising money to be loaned to its members, and others, shall be known in this chapter, and in the laws relating to the bureau of building and loan associations, as a "building and loan association," or as a "savings association." Associations organized under the laws of this state shall be known as "domestic" associations, and those organized under the laws of other states or territories, as "foreign" associations. Associations may be organized and conducted under the general laws of Ohio relating to corporations, except as otherwise provided in this chapter. (99 v. 528 1.)

Name.

Sec. 9644. The name of every such corporation hereafter organized, or heretofore organized and hereafter changing its name, shall begin with any word it may select, and end with the word "company" or with the word "association." It also shall use its name in any order it designates, and if it so desires, with other words not forbidden by law, any one or more of the following words, or combination of words, at its option: "Savings", "building", "loan", "savings and loan", or "building and loan." But such association shall not use the words "bank", "banking" or "trust" nor any one or more of them in combination. (99 v. 528 2.)

When Business May Be Commenced.

Sec. 9645. The capital stock named in the articles of incorporation shall be deemed to refer to the authorized capital. The organization may be completed and business commenced when five per cent thereof is subscribed, and the names and addresses of its officers and not less than two copies of its constitution and by-laws have been filed with the inspector of building and loan associations. (99 v. 528 3.)

Directors, Term of Office.

Sec. 9646. Directors may be elected for any term, not less than one year nor longer than three years. If such term be longer than one year, it shall be so arranged that as nearly as may be, the term of office of an equal number of directors will expire each year. (99 v. 528 4.)

Powers.

Sec. 9647. Such corporation shall have all the powers set forth in the following sections of this chapter. (99 v. 528 5.)

Receiving of Deposits; Joint Accounts.

Sec. 9648. To receive money on deposits, and all persons, firms, corporations and courts, their agents, officers and appointees may make such deposits and stock deposits, but such corporation shall not pay interest thereon exceeding the legal rate. When such deposits or stock deposits are made to the joint account of two or more persons, whether adults or minors, with a joint order to the corporation that such deposits or any part thereof are to be payable on the

order of any one or more of such joint depositors, and to continue to be so payable notwithstanding the death or incapacity of one or more of the persons making them, such account shall be payable to any one or more of such survivors or survivor or order notwithstanding such death or incapacity. No recovery shall be had against such corporation for amounts so paid and charged to such account. (99 v. 528 6.)

Issue of Stock: Vote.

Sec. 9649. To issue stock to members on such terms and conditions as the constitution and by-laws provide. Each member may vote his stock in whole or fractional shares, as the constitution and by-laws provide, but no person shall vote more than twenty shares in any such corporation in his own right, nor have the right to cumulate his votes. But every subscriber for stock in accordance with the constitution of the association, may vote the amount of stock so subscribed for, in no event to exceed twenty shares. (99 v. 529 7.)

Assessments.

Sec. 9650. To assess and collect from members and others, such dues, fines, interest and premium on loans made, or other assessments, as may be provided for in the constitution and by-laws. Such dues, fines, premium or other assessments shall not be deemed usury, although in excess of the legal rate of interest. (99 v. 529 8.)

Withdrawal of Stock Deposits.

Sec. 9651. To permit members to withdraw all or part of their stock deposits, at such times, and upon such terms as the constitution and by-laws provide.

Any member, however, who withdraws his entire stock deposit, or whose stock has matured, shall be entitled to receive all dues paid in and dividends declared thereon, less all fines or other assessments, and less the pro rata share of all losses, if any have occurred. (99 v. 529 9.)

Withdrawal of Deposits.

Sec. 9652. To permit withdrawal of deposits upon such terms and conditions as the association provides except by check or draft. But no such association shall be permitted to carry for any member or depositor any demand, commercial or checking account. Nothing in this chapter shall prevent members or depositors from withdrawing funds by non-negotiable orders. (99 v. 529 9.)

Cancellation.

Sec. 9653. To cancel shares and parts of shares of stock upon which the credits have been withdrawn, or upon which loans have been repaid, and re-issue them as new stock. (99 v. 529 10.)

Rules as to Minors.

Sec. 9654. To issue stock to minors and receive deposits thereon and permit both stock and deposits to be withdrawn, transferred, pledged and voted by such minors as other stock and stock deposits; to receive deposits of money by or for minors and to pay them to such minors, or upon their order. The receipt or paid order of such minor, therefor, shall be a valid acquittance of the rights of all concerned. (99 v. 529 11.)

Property, Leasing, Holding of.

Sec. 9655. To lease, acquire, hold, encumber, convey and rent such real estate and personal property as is necessary for the transaction of its business, or necessary to enforce or protect its securities. (99 v. 529-12.)

Borrowing Money.

Sec. 9656. To borrow money, not exceeding twenty per cent of the assets, and issue its evidence of indebtedness or other security therefor. (99 v. 530-13.)

Loans.

Sec. 9657. To make loans to members and others on such terms, conditions and securities as may be provided by the association. (99 v. 530-14.)

Cancellation of Loan.

Sec. 9658. To cancel such loans and release the securities on such terms as the board of directors provide. But any member may have his loan cancelled upon the following terms: After the premium for one year has been paid, and also the interest and premium up to the date of cancellation, the borrower shall pay the sum actually borrowed less the dues paid and dividends credited, and also any fines or other assessments required by the constitution and by laws. (99 v. 530-15.)

Reserve and Undivided Profit Fund.

Sec. 9659. To accumulate from the earnings a "reserve fund" for the payment of contingent losses, and

an "undivided profit fund", both of which may be loaned and invested as other funds of the association. (99 v. 530-16.)

Idle Funds, How Invested.

Sec. 9650. To invest any of its idle funds, or any part thereof, in bonds or interest bearing obligations of the United States, or of the District of Columbia, or of the State of Ohio, or of any county, township, school district, or other political division in the State of Ohio, or of any incorporated city or village, in the State of Ohio, and in such other securities as now are or hereafter may be accepted by the United States to secure government deposits in national banks. But such investments at no time shall amount in the aggregate to more than twenty per cent of the assets of such corporation. (99 v. 530-16.)

May Deposit Idle Funds.

Sec. 9651. To deposit any of such funds or part thereof, in any financial institution that is subject to inspection by the United States, or by the state of Ohio; and receive therefor certificates of deposit. (99 v. 530-16.)

Purchase Interest bearing Obligations, Sale of to Close Up Business Permitted.

Sec. 9652. To buy but not to sell, except whenever it desires to terminate and close up its business affairs or in case of financial emergency, and then only with the consent previously had of the inspector of building and loan associations, interest bearing obligations secured by real estate mortgages, which shall in all respect comply with, and be within the rules adopted

for making mortgage loans by the corporation making such investments. Such mortgage investments may be held and reported as mortgage loans. (106 v. 431.)

Distribution of Earnings.

Sec. 9663. To make such annual or semi-annual distribution of the earnings as is hereinafter provided, and as the constitution and by-laws may prescribe. (99 v. 530-17.)

Certificate of Increase, Decrease, etc., Where Filed.

Sec. 9664. To increase or decrease its authorized capital or the face value of its shares, or change the name of the corporation by a majority vote of its board of directors. A certificate of such action shall be made by the president and secretary, and duly filed with the secretary of state, after which in the use of the changed stock and changed name, all rights of all parties shall remain the same as before such change was made. (99 v. 530-18.)

Dissolution.

Sec. 9665. To dissolve the corporation when by a majority vote of the stock entitled to be voted under its constitution and by-laws, which shall be consistent with the provisions of section ninety six hundred and forty nine, its continuance is deemed to be no longer desirable, but subject to the contract rights of its borrowers, and the vested rights of its members. (99 v. 531-19.)

Amendment of Articles.

Sec. 9666. To amend its articles of incorporation, and increase or decrease the number of its directors, by complying with all the requirements provided in

its own constitution for the amendment thereof. The other officers of such corporation shall consist of a president, one or more vice presidents, one or more secretaries, and such others as its constitution and by-laws provide. (99 v. 531-20.)

Constitution and By-Laws.

Sec. 9667. To provide, by constitution adopted by its members, and by laws adopted by its board of directors, for the proper exercise of the powers herein granted, and the conduct and management of its affairs. (99 v. 531-21.)

Other Powers.

Sec. 9668. To have all such other powers as are necessary and proper to enable such corporation to carry out the purpose of its organization. (99 v. 531-22.)

Banks, Designation of, to Receive Funds.

Sec. 9669. The board of directors shall designate a bank or banks, in which it shall cause the funds of such corporation to be deposited in its name. Such funds when so deposited, can be withdrawn only in such manner and for such purpose as is provided in the constitution and by-laws and authorized by law. (99 v. 531-23.)

Bond of Officers.

Sec. 9670. All bank books showing such deposits shall be open to the inspection of any director at any time. All officers of such association who have charge or possession of moneys, securities, or property, shall give bond before entering upon their duties, to the satisfaction of the board of directors, for the faithful performance thereof, and the safe keeping and proper

application of all moneys or property coming into their hands. All officers of such corporations on being re-elected to office shall renew their bonds. The bond may be increased or additional securities required at any time by the board of directors. Directors shall not be eligible as bondsmen, but shall be individually liable for any loss to members, caused by their neglect to comply with the provisions of this and the preceding sections. (99 v. 531-23.)

Reserve Fund.

Sec. 9671. The amount to be set aside to the reserve fund, for the payment of contingent losses shall be determined by the board of directors, but in all permanent or perpetual associations, at least five per cent of the net earnings shall be set aside each year to such fund until it reaches at least five per cent of the total assets. All losses shall be paid out of such fund until it is exhausted. When the amount in such fund falls below five per cent of the assets as aforesaid, it shall be replenished by annual appropriations of at least five per cent of the net earnings as hereinbefore provided until it again reaches such amount. (99 v. 531-24.)

Expenses; How Paid.

Sec. 9672. All expenses of such association shall be paid out of the earnings only, and so much of the earnings as may be necessary must be set aside each year for such purpose. But charges incident to a loan, if paid by the borrower, shall not be deemed a part of the current expenses. (99 v. 532-25.)

Dividends.

Sec. 9673. After payment of expenses and interest, a portion of the earnings to be determined by the board of directors, annually or semi-annually, shall also be

placed in the reserve fund for the payment of contingent losses, as hereinbefore provided, and a further portion of such earnings to be determined by the board of directors, shall be transferred as a dividend annually or semi-annually, in such proportion to the credit of all members as the corporation by its constitution and by-laws provides, to be paid to them at such time and in such manner in conformity with this chapter as the corporation by its constitution and by-laws provides. Any residue of such earnings may be held as undivided profits to be used as other earnings, except that such undivided profit fund at no time shall exceed three per cent of the total assets of the association. (99 v. 532 25.)

Losses.

Sec. 9674. All losses shall be assessed in the same proportion and manner on all members after the amounts in the reserve fund and the undivided profit fund have been applied to the payment thereof. (99 v. 532 25.)

Listing of Shares for Taxation.

Sec. 9675. The shares and loans advanced to its members shall be exempt from taxation, except that shares of stocks upon which no loans have been made or money advanced by the company, shall be considered and held as credits. The members individually shall list for taxation the number of shares held by them, and the true value thereof in money, on the day preceding the second Monday in April each year, and they shall be assessed at such valuation for taxation and taxes as other property. (99 v. 532 26.)

Inspection.

Department of Building and Loan Associations.

Inspector of Building and Loan Associations.

Sec. 674. The governor with the advice and consent of the senate, shall appoint an inspector of building and loan associations, who shall serve for a term of three years. No such inspector of building and loan associations shall have any official connection with a building and loan association, or be interested in the business thereof, except as a stockholder. (103 v. 181 1.)

Bond, Oath and Approval.

Sec. 675. Before entering upon the discharge of the duties of his office the inspector of building and loan associations shall give a bond to the state in the sum of ten thousand dollars with two or more sureties or with a surety company authorized to do business in the state of Ohio, approved by the governor, conditioned for the faithful discharge of the duties of his office. Such bond, with the approval of the governor and the oath of office endorsed thereon, shall be deposited with the secretary of state and kept in his office. (103 v. 181 2.)

Duties of Inspector.

Sec. 676. The inspector of building and loan associations shall see that the laws relating to building and loan associations are duly executed and enforced. When a violation of a law relating to building and loan associations is reported to him he shall take, or cause to be taken, the testimony, under oath, of any and all persons supposed to have any knowledge of such violation, and cause such testimony to be reduced to writ

ing. If he be of the opinion that there is sufficient evidence, he shall cause the person suspected of such violation to be arrested and charged with such offense, and shall furnish the attorney general or the proper prosecuting attorney with the information obtained by him, the names of the witnesses and a copy of all material testimony taken in the case. (103 v. 181-3).

Deputies.

Sec. 677. With the approval of the governor, the inspector of the building and loan associations may employ from time to time, the necessary deputies, assistants, clerks and examiners, to assist him in the discharge of the duties imposed upon him by law. With such approval he may remove any such clerk or examiners at any time. (103 v. 182 4.)

Salary of Inspector.

Sec. 677 1. The salary of the inspector of building and loan associations shall be three thousand six hundred dollars, per annum, and shall be paid at the same time as the heads of other state departments. (103 v. 182 5.)

Salaries of Deputies, Assistant, etc.

Sec. 677 2. The inspector of building and loan associations shall fix the salaries of the deputies, assistants, clerks and examiners at such rates per annum as the governor shall approve. Upon vouchers approved by the inspector of building and loan associations, such salaries shall be paid by the treasurer of state, upon the warrant of the auditor of state. (103 v. 182 6.)

Expenses.

Sec. 677-3. The actual and necessary traveling expenses of the inspector of building and loan associations, and of the deputies, assistants, clerks and examiners, incurred in the discharge of their official duties shall be paid monthly by the treasurer of state, upon the warrant of the auditor of state. Vouchers therefore shall be fully itemized, approved by the inspector of building and loan associations, and countersigned by the auditor of state. (103 v. 182 7.)

Sec. 674-4. All expenses incurred by the inspector of building and loan associations, in the performance of the duties imposed upon him by law, including the salary of such inspector, his deputies, assistants, clerks and examiners, shall be paid from funds appropriated therefor. (103 v. 182 8.)

Seal.

Sec. 677-5. The seal of the inspector of building and loan associations shall be one and three-fourths inches in diameter, shall have engraved thereon the coat of arms of the state, and shall be surrounded by the words, "Inspector of Building and Loan Associations of Ohio." (103 v. 182 9.)

All Instruments Sealed With the Seal Received in Evidence.

Sec. 677-6. Every certificate or other instrument executed, or order made, by the inspector of building and loan associations, in pursuance of any authority conferred upon him by law, and sealed with the seal of his office, or copies thereof duly authenticated under such seal, shall be received in evidence in all courts of this state. (103 v. 182 10.)

Place of Office.

Sec. 677 7. The inspector of building and loan associations shall be furnished by the state with suitable rooms, at the seat of the government, for conducting the business of his office. (103 v. 182 11.)

Foreign Associations.

Requirements from Foreign Associations.

Sec. 678. Foreign building and loan associations doing business in this state shall conduct such business in accordance with the laws governing domestic associations. No foreign building and loan association shall do business in Ohio until it procures from the inspector of building and loan associations a certificate of authority to do business in this state after complying with the following provisions:

1. It shall deposit with the inspector one hundred thousand dollars, in cash or bonds of the United States or this state, or of a county or municipal corporation therein, satisfactory to the inspector.

2. It shall file with the inspector a certified copy of its charter, constitution and by-laws, and other rules and regulations showing its manner of conducting business together with a statement such as is required annually from all associations.

3. It shall also file with the inspector a written instrument, duly executed, agreeing that a summons may issue against it from any county in this state directed to the sheriff of the county in which the office of inspector is situated, commanding him to serve it by certified copy personally upon the inspector or by leaving a copy thereof at his office. The inspector shall mail a copy of any papers served on him to the home office of such association. (99 v. 533 31.)

Certificate of Authority to Do Business.

Sec. 679. When a foreign building and loan association has complied with the provisions of the preceding section, and the inspector is satisfied that it is doing business according to the laws of Ohio, and is in sound financial condition, he shall issue his certificate of authority to the association to do business in this state. Annually thereafter, upon filing the annual statement herein provided for, if the inspector is satisfied as herein provided, he shall issue a renewal of such certificate. (99 v. 533 32.)

Collection of Interest and Exchange of Securities.

Sec. 680. A foreign building and loan association may collect and use the interest on securities deposited as provided by law so long as it fulfills its obligations and complies with the laws of this state. It may also exchange them for other securities of equal value satisfactory to the inspector. (99 v. 534 33.)

Securities Liable for Claimants.

Sec. 681. The deposit made by a foreign building and loan association with the inspector of building and loan associations shall be held as a security for all claims of residents of this state against such association, and be liable for all judgments or decrees thereon, and subjected to the payment thereof in the same manner as the property of other non-residents. Should an association cease to do business in this state, the inspector may release securities in his discretion, retaining sufficient to satisfy all outstanding liabilities. (99 v. 534 34.)

See also Section 178 of the General Code of Ohio.

Annual Reports.

Sec. 682. Every building and loan association doing business in this state, annually, at the end of each fiscal year or within forty days thereafter, shall make a full and detailed report in writing of the affairs and business of the association for the preceding year, and showing its financial condition at the end thereof. With the first report made by an association it shall file a certified copy of its constitution and by-laws, or other rules and regulations, showing its manner of doing business. (99 v. 534-35.)

Form of Report.

Sec. 683. The report required in the preceding section shall be the form and contain such information as is prescribed by the inspector of building and loan associations. It shall be sworn to by the secretary and its correctness attested by at least three directors or an auditing committee appointed by the board. The original shall be filed with the inspector of building and loan associations within forty days after the close of the fiscal year. Such an abstract therefore as the inspector requires shall be posted for sixty days in the office or meeting place of such association, and published in a newspaper regularly issued in the county in which it is located. (99 v. 534-36.)

Examination of Associations.

Annual Examination.

Sec. 684. At least once each year the inspector of building and loan associations shall make an examination into the affairs of each such association, or cause it to be made by a person appointed by him for that purpose. (99 v. 534-37.)

Expenses of Examination.

Sec. 685. The expenses of all examinations shall be paid by this state, except that when, by the laws of any other state, district, territory or nation, examinations of such associations of this state are required or permitted to be made by any official or other authority of such other state, district, territory or nation at the expense of such associations, then the expenses of all such examinations made by the inspector of this state, of such associations of that state, district, territory or nation, must be respectively charged to and collected from such associations so examined. (99 v. 534 37.)

Revocation of Charter for Illegal Practices.

Sec. 686. If upon examination, the inspector of building and loan associations finds any domestic association conducting its business in whole or part contrary to law, or failing to comply therewith, he shall notify the board of directors of such association of such fact in writing. If, after thirty days, such illegal practices or failure continue, he shall communicate the facts to the attorney general, who shall cause proceedings to be instituted in the proper court to revoke the charter of such association. (99 v. 535 38.)

Dissolution if Condition Unsound.

Sec. 687. If, upon examination, the inspector of building and loan associations finds that the affairs of a domestic building and loan association are in an unsound condition, and that the interest of the public demand its dissolution and the winding up of its business, he shall so report to the attorney general, who shall institute the proper proceedings for that purpose. (99 v. 535 39.)

Powers of Examiners.

Sec. 688. An examiner appointed by the inspector of building and loan associations, under the provisions herein relating to such associations, shall have access to and may compel the production of all books, papers, securities, moneys and other property of an association under examination. He may administer oaths to, and examine the officers and agents of such association as to its affairs. (99 v. 535-40.)

Inspector May Publish Result.

Sec. 689. If the inspector of building and loan association deems it to the interest of the public, he may publish the results of such examination in a newspaper of general circulation in the county in which such association is located, if it is a domestic association, and in some newspaper in the city of Columbus if it is a foreign association. (99 v. 535-41.)

May Cancel Authority of Foreign Association.

Sec. 690. If upon examination the inspector of building and loan associations finds that a foreign association does not conduct its business in accordance with law, or that its affairs are in an unsound condition, or if it refuses to permit an examination to be made, he may cancel its authority to do business in this State, and cause a notice thereof to be mailed to the home office of the association and published in at least one newspaper published in the city of Columbus. After the publication of such notice no such association or agent thereof shall receive further stock deposits from members residing in this state, except payments on stock on which a loan has been taken. (99 v. 535-42.)

Fees.

Fees to be Paid to Inspector.

Sec. 691. Foreign building and loan associations shall pay to the inspector of building and loan associations the following fees:

For filing an application for admission to do business in this State, five hundred dollars;

For each certificate of authority and annual renewal thereof, two hundred dollars.

Every building and loan association doing business in this State, whether foreign or domestic, shall pay to the inspector of building and loan associations, for filing each annual report, at the time said annual report is filed, the sum of ten dollars, and in addition thereto, one-eightieth of one per cent of its assets, as shown in such report. All such fees collected shall be paid into the general revenue fund. (106 v. 236.)

Securities to be Deposited With Treasurer of State.

Sec. 692. All securities or cash deposited with the inspector of building and loan associations shall be deposited with the treasurer of State, who, with his sureties, shall be responsible for the safe keeping thereof. The treasurer shall deliver such securities only upon the written order of the inspector. (99 v. 536-44.)

Dissolution or Consolidation of Building and Loan Associations.

Sec. 693. A building and loan association or a savings association may provide in its constitution and by-laws for the time and terms of its dissolution and for its consolidation with one or more of such corporations on terms and conditions to be determined

upon by their board of directors. In case of the dissolution of such a corporation, its board of directors by a majority vote may be authorized to sell and transfer its mortgage securities or other property, or both, to another corporation, person or persons, subject to the vested and accrued rights of the mortgagors. (99 v. 537-48.)

Penalties.

Forfeiture for Non-compliance.

Sec. 694. A building and loan association which does business in this State without first complying with the provisions herein or which violates or fails to comply with provisions of law relating to building and loan associations shall forfeit and pay not less than fifty dollars nor more than one thousand dollars, to be recovered by an action in the name of the State and on collection paid into the State treasury. (99 v. 536-45.)

Record of Proceedings of Inspector—Report.

Sec. 695. The inspector of building and loan associations shall keep and preserve in permanent form a full record of his proceedings, including a concise statement of each association examined, and, in his annual report, he shall report the general conduct and condition of the building and loan associations doing business in this State. Such report shall include the information contained in the statements required of the associations in tabulated form. (106 v. 510.)

Embezzlement by Officer of Building and Loan Association.

Sec. 12472. Whoever, being a president, director, trustee, member of a committee, secretary, treasurer,

attorney or other officer or agent of a building and loan association or savings association as provided by law, embezzles, abstracts or willfully misapplies any of the moneys, funds or credits thereof, or issues or puts into circulation a warrant or other order, or assigns, transfers, cancels or delivers a note, bond, draft, mortgage, judgment, decree or other written instument belonging thereto, or raises money otherwise, or receives money from a member or other person for and in the name of such association unless authorized so to do by the board of directors thereof, shall be imprisoned not less than one year nor more than ten years and be liable to the person injured thereby to the extent of the damage incurred. Suit may be brought against the person so violating and the sureties on his bond given to such association for the faithful performance of his duty. (99 v. 536-46.)

Signing Name to Order Without Authority.

Sec. 13188. Whoever, being a president, director, trustee, member of a committee, secretary, treasurer, attorney or other officer or agent of a building and loan association or savings association, as provided by law, signs the name of a person to an order or warrant for the payment of money without proper power of attorney or written order from the person to whose order such order or warrant is made payable, shall be imprisoned not less than one year nor more than ten years. (99 v. 536-46.)

Declaring Dividend Greater than Earned.

Sec. 13189. Whoever, being a member of a board of directors of a building and loan association or savings

association, as provided by law, votes to declare, or, being a financial or first secretary thereof, declares or advises the board of directors thereof to declare a greater dividend than has been actually earned by such association, for the purpose of deceiving the people or defrauding the members thereof, shall be imprisoned not less than one year nor more than ten years. (99 v. 536-46.)

False Entry in Book, etc.

Sec. 13190. Whoever, being a member of a board of directors of a building and loan association or savings association, as provided by law, certifies to, or makes a false entry on a book, report or statement of or to such association, with intent to deceive, injure or defraud it or another company, body politic or corporate or person, or to deceive any one appointed to examine the affairs of such association, shall be imprisoned not less than one year nor more than ten years. (99 v. 536-46.)

Aiding Officer to Violate Preceding Sections.

Sec. 13191. Whoever, with intent to deceive, injure or defraud a building and loan association or savings association, as provided by law, or other company, body politic or corporate or person, aids or abets a president, secretary, treasurer, committee or other person in violation of any of the next four preceding sections shall be imprisoned not less than one year nor more than ten years. (99 v. 536-46.)

Failing to Make Reports, etc.

Sec. 13192. Whoever, being an officer thereof, fails to make the reports required of him by the laws provided for the organization, regulation and inspection of building and loan associations or savings associations, or, being an officer, employee or other person,

solicits business for, aids or assists such association to do business contrary to the provisions of such laws, or without having complied therewith, shall be fined not more than five hundred dollars or imprisoned not more than six months, or both. (99 v. 536-46.)

Liability on Bond.

Sec. 13193. Whoever violates any provision of the next five preceding sections shall be liable to the person injured thereby to the extent of the damage incurred and suit may be brought against the person so violating and the sureties on the bond given by him to such association for the faithful performance of his duty. Fines collected under the next five preceding sections shall be paid into the State treasury. (99 v. 536-46.)

"TREASURY DEPARTMENT,

Office of

COMMISSIONER OF INTERNAL REVENUE

WASHINGTON, *Jan.* 30, 1918.

Mr. GEO. S. WALKER,
Building and Loan Commissioner,
604-606 Claus Spreckels Bldg.,
San Francisco, Calif.

SIR:

Receipt is acknowledged of your letter of the 18th instant, in which you ask to be advised whether or not Building and Loan Associations having a permanent guarantee capital and those loaning money to others than members of the Association are exempt under the provisions of the Act of September 8, 1916, and Titles I and II of the Act of October 3, 1917.

In this connection the following extracts from your letter are quoted:

First. Under the laws of this and one or two other States, Building and Loan Associations may have a permanent guarantee capital stock, which is nonwithdrawable, and in practice participates in common with installment shares, besides which it receives a bonus, in some cases equal to one (1) per cent of the average loans in force. The law provides that this stock shall be subject to all the conditions and liabilities attaching to the paid-in capital stock of other classes of corporations, and shall protect and guarantee all other stockholders and creditors against any loss.

Second. Under the laws of this and certain other States, Building and Loan Associations may—and in very many cases do—loan to others than shareholders or members; and especially is this the case where they have a permanent guarantee capital, and the working capital comes from other sources than installment and full paid-up shares.

In reply you are informed that Building and Loan Associations organized and operated in accordance with the laws of the State in which they are organized and do business are exempt from the provisions of the law referred to above. Therefore, if a Building and Loan Association in your State, which transacts business in accordance with the information contained in your letter, does so under the authority conferred upon it by the laws of the State of California, then that fact does not destroy its exemption under the provisions of the acts cited.

Respectfully,

DANIEL C. ROPER,
Commissioner."

IN THE

Supreme Court of the United States

No. 46

THE UNITED STATES, PETITIONER,

v.

THE CAMBRIDGE LOAN AND BUILDING COMPANY

MOTION FOR LEAVE TO FILE BRIEF AMICI CURIAE AND BRIEF

The undersigned Cleveland E. Cross and Herbert W. Nantz show to the court that they are counsel for the appellants in the cases of *The Home Savings and Loan Co. v. Commissioner of Internal Revenue*, and *The Henderson Savings and Loan Co. v. Commissioner of Internal Revenue*, now pending in the United States Circuit Court of Appeals for the Sixth Circuit on petition for review of the decisions of the United States

Board of Tax Appeals; that those cases present issues involving the construction of Sections 231 (4) of the Revenue Acts of 1918 and 1921, the decision of which will probably be ruled by the decision of this court in this case; that counsel for both parties have consented in writing to the filing by the undersigned of a brief *amici curiae*, and their consents have been filed with the clerk of this court.

Wherefore, the said Cleaveland R. Cross and Herbert W. Nauts pray leave to file herein and submit for consideration the following brief *amici curiae*:

ARGUMENT

I

The Term "Domestic Building and Loan Associations," as Employed in the Revenue Act of 1918, Includes Every Association Designated or Known as a Building and Loan Association by State Laws.

The Revenue Act of 1918, Title II, Part III, providing for corporation income taxation, contains the following:

> "Sec. 231. That the following organizations shall be exempt from taxation under this title * * *:
>
> (4) Domestic building and loan associations and co-operative banks without capital stock organized and operated for mutual purposes and not for profit;"

The statute quoted does not define "building and loan associations." In formulating a definition, it is important and even controlling to know what were gener

ally recognized as building and loan associations at the time of the enactment of the statute in question. The most fertile source of such information is found in the statutes of the several states providing for the organization and regulation of building and loan associations.

An examination of the state laws in force at the time of the enactment of the Revenue Act of 1918, and for some years previous thereto shows that building and loan associations were recognized as a special class of corporations in all the states. (Note 1.)

Note 1.

Ala., Ch. 69, Art. 17, code 1907;
Ark., Sec. 780, St. 1921;
Ariz., Title IX, Ch. 3, code 1913;
Calif., Sec. 648, Civ. code 1923;
Colo., Ch. XLIV, Comp. Laws;
Conn., Title XXXIV, Ch. 208, Gen. St. 1918;
Del., Ch. 65, Art. 3, code 1915;
Fla., Secs. 4207-4242, Rev. Gen. St.;
Ga., Secs. 2878-2882, code 1911;
Idaho, Ch. 200, Comp. St. 1919;
Ill., Ch. 32, Sec. 78, Rev. St. 1911;
Ind., Ch. 27, Art. 1, Burns' Ann. St. 1926;
Ia., Title XX, Comp. code 1919;
Kan., Ch. 17, Rev. St. 1923;
Ky., Sec. 854, Carroll's St.;
La., Secs. 760-784, Marr's Ann. Rev. St.;
Me., Ch. 52, Rev. St. 1916;
Md., Sec. 134, Art. 23, Ann. code 1911;
Mass., Ch. 170, A. L. 1921;
Mich., Ch. 191, Comp. L.;
Minn., Secs. 7740-7770, Gen. St. 1923;
Miss., Ch. 87, Hemingway's Ann. code 1917;
Mo., Ch. 90, Art. IX, R. S. 1919;
Mont., Part III, Ch. 24, R. C. 1921;
Neb., Title V, Art. XX, Comp. St. 1922;
Nev., Act of Mar. 24, 1915;
N. H., Ch. 290, Pub. L. 1926;
N. J., Comp. St., p. 333;
N. M., Ch. XV, St. 1915;
N. Y., Ch. 5, Secs. 375-420, Cahill's Cons. L.;
N. C., Ch. 91, Art. 15, St. 1919;
N. D., Ch. 26, Civ. code, Comp. L. 1913;
Ohio, Title IX, Div. IV, Ch. 1, Civ. code;
Okla., Ch. 34, Art. 7, Comp. St. 1921;
Oregon, Title XXXIX, Ch. V, L. 1920;
Penn., Sec. 2419, St. 1920;

In all states but two they were classified as business corporations or corporations for profit, having a capital stock divided into shares. In the two states referred to, Idaho and California, they apparently might be organized with or without capital stock. (Note 2.)

By the statutes of 43 of the states building and loan associations were expressly denominated as such. In Arizona and New York they were classified with and denominated savings and loan associations. In Massachusetts they were denominated co-operative banks. In Idaho they were denominated land and building corporations. In Vermont they were denominated co-operative savings and loan associations.

In addition to installment or running stock, associations were authorized to issue paid-up or prepaid stock in 23 states. (Note 3.)

R. I., Ch. 265, Gen. L. 1923;
S. C., Sec. 811, Art. 26, Civ. code;
S. D., Sec. 9066, Rev. code 1919;
Tenn., Sec. 2128, Ann. code 1917;
Tex., Ch. 25 A, Complete St. 1920;
Utah, Ch. 9, Title 19, Comp. L. 1917;
Vt., Ch. 229, Title 28, Gen. L. 1917;
Va., Ch. 166, Title 37, code 1919;
Wash., Secs. 4565-4598, code 1919;
W. Va., Sec. 2924, code 1913;
Wis., Ch. 93, St. 1919;
Wyo., Ch. 331, Comp. St. 1919.

Note 2.

Idaho, Sec. 3046, Comp. L.;
Calif., Sec. 6489, Civ. code 1923.

Note 3.

Ariz., Sec. 2121, code 1913;
Colo., Sec. 2792, Comp. L.;
Del., Sec. 1927, Rev. code 1915;
Fla., Sec. 4214, Rev. Gen. St.;
Ga., Sec. 2823, code 1911;
Idaho, Sec. 4006, Comp. St. 1919;
Ind., Sec. 5083, Burns' Ann. St. 1926;
Iowa, Sec. 5845, Comp. code 1919;
Kan., Sec. 2214, Gen. St. 1915;

In twelve states associations were expressly authorized to issue various other classes of stock, including permanent, preferred and guaranteed stock. (Note 4.)

Associations had the unrestricted power to borrow money in fourteen states. (Note 5.)

Ky., Sec. 856 (a), Carroll's St.;
La., Sec. 763, Ann. St.;
Md., Sec. 137, Ann. code 1911;
Mass., Sec. 12, A. L. 1921;
Minn., Sec. 7751, Gen. St. 1923;
Miss., Sec. 3916, Ann. code 1917;
Mo., Sec. 20201, R. S. 1919;
N. Y., Sec. 383, Cons. L.;
N. C., Sec. 5177, St. 1919;
Ohio, Sec. 9649, Gen. code;
Oregon, Sec. 6935, L. 1920;
R. I., Sec. 3903, Gen. L. 1923;
S. C., Sec. 4016, Civ. code 1922;
S. D., Sec. 9071, code 1919.

Note 4.

Ark., Sec. 1703;
Calif., Sec. 323, Civ. code 1923;
Del., Sec. 1927, code 1915;
Ga., Sec. 2823, code 1911;
Idaho, Sec. 4752, Comp. St. 1919;
Kan., Sec. 2214, Rev. St. 1923;
Ky., Sec. 856 (a), Carroll's St.;
La., Sec. 763, Marr's Ann. St.;
N. C., Sec. 5177, St. 1919;
R. I., Sec. 3903, Gen. L. 1923;
S. D., Sec. 9071, Rev. code 1919;
Tenn., Sec. 2051 (a) 1, Ann. code 1917.

Note 5.

Ark., Sec. 1717, St. 1921;
Calif., Sec. 325, Civ. code 1923;
Del., Sec. 2, Ch. 25, Art. 1, code 1915;
Ga., Sec. 2823, code 1911;
Idaho, Sec. 4907, Comp. St. 1919;
Ind., Sec. 5091, Burns' Ann. St. 1926;
La., Sec. 762, Marr's Ann. Rev. St.;
Md., Sec. 7, Art. 23, code 1911;
Mass., Sec. 16, Ch. 170, A. L. 1921;
Miss., Sec. 4073, Hemingway's code 1917;
N. D., Sec. 5131, Comp. L. 1913;
Oregon, Sec. 6926, L. 1920;
R. I., Sec. 3470-I, Gen. L. 1923;
Tenn., Sec. 2054, Ann. code 1917.

In eleven states the amount of money which might be borrowed was limited to a specified proportion of the assets, varying from 10% to 80%. (Note 6.)

In two states the amount of money which might be borrowed was limited to a specified proportion of the paid in capital. (Note 7.)

In four states the amount borrowed was limited to a specified proportion of the dues, installments or interest paid in. (Note 8.)

In Washington the amount of borrowed money was limited to a proportion of the loans made. (Note 9.)

In Pennsylvania an association might borrow an amount not exceeding 25% of its withdrawals. (Note 10.)

Note 6

Colo., Sec. 2795, Comp. L.;
Conn., Sec. 4017 (6), Gen. St. 1918;
Fla., Sec. 4221, Rev. Gen. St.;
Ill., Sec. 82 (b), Rev. St. 1911;
Kan., Sec. 861, Rev. St. 1923;
Minn., Sec. 2751, Gen. St. 1923;
Mont., Sec. 6358, R. C. 1917;
Ohio, Sec. 9656, Gen. code;
S. C., Sec. 824, Civ. code;
S. D., Sec. 9075, Rev. code 1919;
Wis., Sec. 2011, St. 1919.

Note 7

N. Y., Sec. 388, Cons. L.;
Penna., Sec. 2448, St. 1920.

Note 8

Mo., Sec. 10215, R. S. 1919;
N. C., Sec. 5184, Cons. St. 1919;
N. H., Sec. 13, Pub. L. 1926;
N. J., Sec. 19, P. S. 1903, p. 462.

Note 9

Wash., Sec. 4546, code 1919.

Note 10

Penna., Sec. 2450 St.

Associations are expressly given the power to receive deposits in seven states. (Note 11.)

Ten states permit associations without limitation to make loans to persons who are not members or stockholders. (Note 12.)

In nineteen states associations might loan to non-members funds which were not required by members. (Note 13.)

Note 11.

Ariz., Sec. 2122, code 1913;
Calif., Sec. 633, Civ. code 1923;
Minn., Sec. 7751, Gen. St. 1923;
Ohio, Sec. 9648, Gen. code;
Oregon, Sec. 6952, L. 1920;
S. C., Sec. 4004, Civ. code 1922;
S. D., Sec. 9067, Rev. code 1919.

Note 12.

Ariz., Sec. 2120, code 1913;
Ark., Sec. 1717, St. 1921;
Calif., Sec. 638, Civ. code;
Ga., Sec. 2878, code 1911;
Idaho, Sec. 4911;
Md., Art. 23, code 1911;
Miss., Sec. 3922, Hemingway's code 1917;
Mo., Sec. 10202, R. S. 1919;
Ohio, Sec. 9643, Gen. code;
Wash., Sec. 4565, code 1919.

Note 13.

Colo., Sec. 2794, Comp. L.;
Del., Sec. 2015, Rev. code 1915;
Fla., Sec. 4218, Rev. Gen. St.;
Ind., Sec. 5087, Burns' Ann. St. 1926;
Mass., Sec. 23, Ch. 170, A. L. 1921;
Mont., Sec. 6358, R. C. 1921;
N. H., Sec. 8, Ch. 166, L. 1901;
N. J., Sec. 24, V. Comp. St., p. 333;
N. M., Sec. 527, St. 1915;
N. Y., Sec. 388, Cons. L.;
N. D., Sec. 5120, Comp. L. 1913;
Okla., Sec. 5399, Comp. St. 1921;
Penna., Sec. 2456, St. 1920;
S. C., Sec. 824, Civ. code;
S. D., Sec. 9075, Rev. code 1919;
Tenn., Sec. 2144, Ann. code 1917;
Texas, Sec. 1313 cc, St. 1920;
Va., Sec. 4145, code 1919;
Wyo., Sec. 5217, St. 1919.

From the foregoing it will be seen that under the statutes of the several states regulating the organization and operation of building and loan associations their powers and practices vary considerably.

Their primary purpose is the same, to furnish the financial means to enable people to acquire homes. Their purpose is accomplished by accumulating from various sources funds which are lent to borrowers, in amounts comparatively large in proportion to the cost of the homes acquired, for long terms at a reasonable cost.

Their function could not be efficiently performed by banks or other financial institutions because of the limitations on the amounts which such institutions may invest for long periods on real estate security and because other institutions will not invest their funds in home loans at times when it is more profitable to use them otherwise.

For those reasons building and loan associations offer an advantageous and dependable means of financing home ownership which without them would not exist. It was because they so encouraged home ownership that they were given the tax exemption benefit, and for no other reason.

This clearly appears from the remarks of the senators who participated in the debate upon Section 231 (4) when it came up in the Senate on October 27, 1921. (Cong. Rec., Vol. 61, Part 7, pp. 6868-6872.)

Authorities generally have agreed that the public welfare is concerned with and promoted by citizens owning their own homes. Legislative enactments have consequently in many states granted financial inducements calculated to increase home ownership. Such induce-

ments have been occasionally provided directly for the home owner or builder. More frequently they have been granted directly to building and loan associations which were recognized as the most efficient agents for increasing home ownership. In many states associations have been favored over other corporations by whole or partial tax exemption. They have been generally exempted from the operation of usury laws. Frequently their incorporation fees or annual franchise fees have been reduced below the amounts paid by other corporations. Sometimes their shares have been exempted from taxation in the hands of the owners, and in some states the shares are exempt from execution. We have been able to find no reported case where a building and loan association has been denied any such privilege because of its special methods of operation, prior to the time the question was raised by the Treasury Department with respect to the federal income tax exemption. The privileges have been considered as categorical, and not subject to the special facts of each case.

Methods employed by associations in carrying out their purpose of assisting in the financing of homes will necessarily differ according to local real estate conditions, wealth and income of home purchasers, building conditions, money market, and other conditions. In addition to the simple lending of money to enable borrowers to acquire homes an association must incidentally engage in other activities. It must first of all obtain the funds with which to make its loans and which, obviously, must come largely from sources other than its borrowers. The association must offer to people with money to invest terms which will induce them to place their money with

the association rather than elsewhere. Funds may be raised by the sale of capital stock. Additional funds may be raised by accepting deposits from those who do not desire to become stockholders.

Methods of operation, depending largely on local conditions, are properly the subject of regulation by state laws. We do not believe that Congress was interested in such methods so long as they were consistent with the subject in which Congress was interested, namely, the encouragement of home ownership.

It is not on the principle of mutuality that they were exempted, or Congress would have expressly qualified them by that term, just as it did, in fact, in qualifying "mutual" savings banks, and "mutual" hail, cyclone, fire insurance companies, ditch or irrigation companies and telephone companies, all of which were likewise exempted by paragraphs (2) and (10) of Section 231.

Strict mutuality, in the sense that the term applies to a mutual insurance company, for instance, is impossible in the operation of a building and loan association. A mutual insurance company provides insurance to all its members and simply divides the cost among them. It does no business other than with its beneficiaries, who are its policy holders. *A building and loan association, on the contrary, must secure most of its funds from others than its beneficiaries, who are its borrowers, and who obviously could not furnish the funds to carry on its business or they would not be borrowers.* Unlike the mutual insurance company, which bears the same relation to all with whom it does business, the building and loan association is the creditor of one class with which it does business, and the debtor of the other class.

The only degree of mutuality which can be required of a building and loan association is that which will further its purpose. It exists when its borrowers participate equally in its benefits and when its transactions are with others to the advantage of its borrowers, to the extent possible under existing business conditions.

The government's contention that transactions by building and loan associations with non-stockholders are subversive of their purpose disregards the idea that loans to non-stockholders constitute an extension of that purpose and not a departure from it. That is, if it be in the interest of the public welfare that stockholders own their homes, it is difficult to perceive why the public welfare is not equally concerned that non-stockholders own their own homes, other conditions being equal.

II

If the Exemption Granted by Section 231 (4) of the Revenue Act of 1921 Be Construed in a More Limited Sense Than the Exemption Granted by the Corresponding Section of the 1918 Act, the More Limited Exemption Should Not Be Given Retrospective Effect.

The argument set forth above, in regard to the construction of Section 231 (4) of the Revenue Act of 1918 is, in the main, applicable to the corresponding section of the 1921 Act. However, if the exemption provided by the 1921 Act should be held to be of narrower application than that of the 1918 Act, we submit that the status of the associations for the period between January 1, 1921,

and November 23, 1921, is determined by the 1918 Act and not by the 1921 Act, as contended by the government. The relations between the associations and their borrowers in cases where loans were made during the period between the two dates mentioned were fixed by their contracts, and the associations had no control over such relations after the contracts were entered into.

An association had no power to compel a borrower to become a stockholder after it had made him a loan as a non-stockholder.

Congress must have had this situation in view at the time the 1921 Act was adopted. From the debates in the Senate relating the Section 231 (4) of the 1921 Act, heretofore referred to, it is apparent that there existed no intention to make the change, if any change were contemplated, retrospective to the first of the year.

The language of Section 231 (4) as finally enacted was that contained in the committee amendment to the bill received from the House, which, after attempts to change it in the Senate, was finally passed in the form reported by the finance committee.

Respectfully submitted,

CLEAVELAND R. CROSS,
HERBERT W. NAUTS.